Free Trade and Social Policy

Edited by:
Glenn Drover

Canadian Council on Social Development

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FREE TRADE
AND
SOCIAL POLICY

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Ottawa/Montreal

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At the University of British Columbia School of Social Work, Jenny Russell and Ann Eden were especially supportive in putting the final text together.

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Glenn Drover
School of Social Work
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FOREWORD

In November 1987, CCSD's Board of Governors reviewed the status of the proposed Free Trade Agreement between Canada and the United States in an effort to assess its potential social policy implications.

The difficulty facing the Board was that the only source of solid information on the agreement's social policy implications was the federal government, and it was saying there were none.

According to official spokespersons, social policy issues had either a) never been discussed, or, b) had been taken off the agenda, depending on when they made their statements, or the audience being addressed. Yet there was ample reason to believe the agreement would affect Canadian social policies, at least eventually. Respected academics and social interest groups were saying that any trade agreement of this significance, whether or not social programs were touched directly, would have an effect through long-term pressures to align or harmonize the major fiscal policies and arrangements which shape social policy decisions.

The agreement itself made no reference to long-term effects and perhaps rightly so. At the same time though, the agreement specifically aimed at expanding international trade in the service sector, and a significant portion of this Canadian sector is made up of social services broadly defined. However, in the official explanatory note accompanying the agreement, the Canadian government suggested that there was a broad exclusion of social services, in that "public services" were not to be considered trading commodities. Yet a reading of the fine print revealed that management of a broad range of health and social services was to be considered part of the agreement. Moreover, many Canadian governments are actively moving social and health services from the public sector into the private profit or non-profit sector, and new social services are

being developed on a commercial basis.

While the Board did not deal specifically with the question of jobs to be gained or lost, it did conclude that a trade agreement which opened up international competition in a broad range of commodities would undoubtedly have a major impact on the labour force. Adjustment programs would be required, even if the government was suggesting that such programs were already in place and could accommodate the additional disruption attributable to the Agreement.

In total the situation left many people, including those who might be inclined to support the agreement as the lesser of two evils -- the other being the damage that might be inflicted by protective U.S. legislation-- with an uneasy feeling that the long-term implications of the agreement were either not being considered or not being discussed. The Board decided to issue a statement decrying the official silence in this regard as an insufficient response to the issues being raised. Moreover, they decided to actively cooperate with other groups and individuals to raise the issues for public discussion.

Consequently we were delighted to work cooperatively with Glenn Drover of the University of British Columbia, to organize a seminar on Free Trade and Social Policy in March of 1988. The seminar was designed to raise questions, to explore potential impact, and to share information.

The papers, essentially as presented by their authors, as well as a summary of the discussions which followed, are reproduced here. I believe they speak for themselves in pointing to key issues, to unanswered questions, and to long-term implications.

Many of the observations are speculative. But they are speculation founded on solid knowledge and experience. Our product may not be definitive in projecting the consequences of this agreement. Indeed it is clear that the political will and the social values of Canadians will be the primary determinant of our future social policy. However, the proposed Free Trade Agreement is clearly a significant element in the future policy climate. It cannot be ignored.

Terrance Hunsley,
Canadian Council on Social Development

INTRODUCTION

Glenn Drover

Before and after signing the free trade agreement with the United States, Prime Minister Brian Mulroney promised that Canadian social programs, which he had earlier labelled a sacred trust, would be safeguarded. This assurance was echoed by editorial writers and some leading economists. Yet, the Prime Minister's convictions and the economists' optimism have not been shared by critics of free trade in the trade union movement, the social policy field and the Council of Canadians. The Canadian Labour Congress has opposed free trade, stating that it would destroy Canada's capacity to mount and maintain universal programs. Leonard Shifrin, a social policy columnist, has argued that unemployment insurance, medicare, and the minimum wage may be jeopardized. Mel Hurtig, the Chairperson of the Council of Canadians, has warned that free trade may lead to harmonization and could ultimately threaten Canada's political sovereignty.

The positions taken by proponents and opponents of the free trade agreement have frequently lacked any systematic investigation of its impact on social policy. The Macdonald Commission, which examined many aspects of free trade, treated social policy as a separate and parallel issue. None of the background studies undertaken by the Commission addressed the relationship between free trade and social policy; neither has any government department, nor any major national research organization. Some economists have briefly examined the question and have suggested a minimal impact on social policy based on economic assumptions about the effects of free trade. But they have provided little evidence to support their case.

Because of the paucity of documentation on free trade and social policy, and the abundance of assertions, the Canadian Council on Social Development invited a group

of experts to a seminar in Ottawa to clarify the issues. Participants included academics, economists, social service personnel, business representatives and political advisors, all of whom had extensive involvement in, or knowledge of, Canada's social services. They were asked to clarify issues and to consider whether the Canada-U.S. Free Trade Agreement (CUSFTA) would lead to social policy harmonization. They were also requested to distinguish, where possible, between general trends toward harmonization and specific pressures resulting from the terms of CUSFTA.

The chapters that follow present the basic findings of the seminar. While the seminar served to clarify a range of policy issues related to subsidies, government procurement, tax harmonization, the exchange rate, international free trade agreements, health and social service management, and labour force adjustment, there was no consensus concerning the specific impact of the free trade agreement on social policy -- in part because many participants were unhappy with the distinction between general and specific pressures toward harmonization. This discomfort stemmed less from the semantics of the distinction than the symbolic importance of the agreement itself. For those who viewed CUSFTA simply as an arrangement to eliminate tariff and non-tariff trade barriers, the distinction was straightforward and useful. For those who considered CUSFTA a turning point for Canadian society, in which social policies would be increasingly market-oriented rather than nationally determined, the distinction was not only inappropriate but misleading. Lise Poulin Simon, an economist from Quebec, stated the dilemma most concisely:

> It is not so much the strategy of free trade which represents the greatest danger for Canadian social policy; it's the fact that it is our only economic policy. Past government failures have made attractive to a certain percentage of the population the philosophy of laissez-faire, the return of the free-market, and the reduction of the welfare state. The principal failure has been our inability to put in place a policy to correct high levels of unemployment and regional disparity.

The term 'harmonization' brought somewhat the same reaction. Derek Hum explained that in the context of free trade, harmonization refers to the obligation of

countries not to use other policies, including social policies, to nullify the economic consequences of the elimination of trade barriers. This definition of harmonization was shared by many of the participants in the seminar. However, others predicted that the Agreement would lead to spillover effects which, over time, would lead to increased pressure to Americanize Canadian programs, not out of economic necessity but largely due to political and business imperatives. For these panelists, it was difficult to cast harmonization strictly in economic terms and compartmentalize the impact of the Agreement.

As papers were presented, and discussion ensued, this fundamental division influenced participants' interpretation of CUSFTA. In attempting to clarify the terms of the Agreement and review critics' concerns regarding the effects of the Agreement on Canada's social programs, the Trade Negotiations Office (TNO) took the position that subsidies for social programs were not countervailable if the services subsidized were generally available. The TNO also explained that the chapter of the Agreement dealing with government procurement applied to federal programs, not provincial initiatives; that the framework for trade in services only applied to a limited range of commercially managed social and health programs; and that Canada had no obligation to provide national treatment of measures affecting the conduct or operation of American business investments in Canada such as day care.

In response to the TNO paper, Geoffrey Norquay affirmed that there was nothing in the Agreement to limit the full exercise of sovereign power in the establishment and maintenance of social programs. Bruce Campbell, Barbara Arneil and Leonard Shifrin disagreed with Norquay's conclusions. They highlighted the lack of any explicit exemption for social programs, the inclusion of a wide range of management services, and the open-ended nature of the Agreement as causes for concern.

Papers by Derek Hum and Glenn Drover dealt with issues around harmonization. Hum distinguished between the social programs he claimed were not vulnerable--such as health, post-secondary education, and old age security -- and those made problematic by CUSFTA, including certain income maintenance proposals and regional/industrial development programs. He also noted that relying on the exchange rate to resolve social policy differences between the two countries downplays

regional variations in Canada that arise from the differentiated complexity of the Canadian economy.

Drover suggested that the free trade agreements of Europe and the Antipodes were not analogous with CUSFTA. Furthermore, while free trade agreements were not directly associated with social policy harmonization in other countries, the European agreements established administrative structures influenced by, and accommodating towards, corporatism. An equivalent institutional spillover between Canada and the U.S., he suggested, is the American corporation.

Lise Poulin Simon, Todd Rutley, Gérald Pelletier and Brian Powell did not dispute the distinctions drawn, but attached differing weights to the various determinants. Poulin Simon stressed the need for a full employment policy to protect social programs. Rutley did not see the business community acting as a negative force for harmonization as a result of CUSFTA. On the other hand, Pelletier stated the business sector would push for less progressive tax changes under the Agreement, thereby undermining funding of social programs. Powell emphasized that rather than worry about harmonization, it was important to focus on services that could assist those who lost under the Agreement.

Dennis Guest and George Tsalikis presented papers on income security, health, and social services. Guest concluded that Canada's capacity to maintain its superior programs depended more upon its ability to maintain a social democratic tradition than upon the terms of the Agreement. Tsalikis pointed out that many pressures toward harmonization in the health field exist outside of the free trade agreement. He argued that the management provisions of the chapter on services in the Agreement enhanced the pressures for harmonization. Pran Manga, Ruth Rose-Lizée, Wilfred Brown and Ken Murdoch interpreted the CUSFTA somewhat differently. Manga saw little to prevent the ongoing provision of medicare, but concluded that new, comprehensive health initiatives would be unlikely in the future. Rose-Lizée challenged the economic assumption underlying the free trade deal and questioned the Agreement's implicit legitimization of commercial social service management. Brown suggested that in the long term, the Agreement would likely have a levelling effect on education. Murdoch expressed similar concern for the management of personal social services.

In the seminar's final paper, Paul Gorecki surveyed Economic Council of Canada studies on labour adjustment problems resulting from the free trade deal. He argued that relative to the amount of adjustment normally taking place in the labour market each year, adjustment problems under CUSFTA would be moderate. He concluded that framework rather than sectoral policies should be used to meet any resulting need. His presentation drew fire from Peter Bakvis, who challenged both the Council studies' numerical assumptions and the policy prescription. Shirley Seward stressed that demographic changes in Canadian society would necessitate sectoral approaches. Ken Hart called for a 'radical' reconsideration of current initiatives.

The seminar generated both consensus and debate concerning the relationship between free trade and social policy. There was agreement that broad-based programs like medicare, pensions and education were least likely to be affected directly by the terms of the Agreement. There was universal recognition that contrary to popular opinion, the management of many social and health programs was in fact included in the Agreement as part of tradeable services. There was also wide acceptance of the need for proactive labour force adjustment policies to assist Canadian workers in dealing with increasing trade liberalization and structural changes in the economy.

The participants differed on where to draw the line between general pressures toward harmonization and CUSFTA-specific pressures. There was a general awareness that all industrialized countries faced pressures to harmonize due to the mobility of capital. However, some participants stated that the rationalization of Canadian industry and continental integration under the free trade agreement would intensify those pressures. Others believed that this process would result in economic growth, and thus protect our social policy system. Similarly, while most participants agreed that Canada's profile in the United States would increase, not all felt that enhanced visibility would make this country a prime target for countervailing action.

The most contentious debate centred around the Agreement's inclusion of the management of health and social services, and what this implied for future negotiations in matters related to government procurement services, investment and monopolies. In the Agreement, the preamble to the services chapter states that health, education and social services are excluded.

At the same time, several participants noted the annex to that chapter lists the management of several health and social programs as services covered by CUSFTA. While nothing in the Agreement requires governments in Canada to purchase commercial management services, and the government procurement chapter actually precludes provincial programs, some participants argued that the inclusion of management services opened the door to privatization and American commercial interests. In addition, further negotiations might open up provincial procurement and expand the list of services covered. If the negotiators were unable to reach an agreement on subsidies, it could potentially lead to a redefinition of terms that would widen the doorway. Other participants claimed that this perspective was too pessimistic and placed little faith in the ability of Canadians to be masters of their own destiny.

A similar dichotomy of opinion arose around the issue of monopolies. Under the Agreement, the U.S. must be notified and consulted before the establishment of any monopoly, such as an eventual pharmacare or dental care plan, for example. Some participants felt that this considerably reduced the possibility for future social or health initiatives. Others disagreed, stating that nothing in the Agreement prevented the governments of Canada from exercising their political right to introduce whatever social programs they wished.

The divergence of opinion among these experts should come as no surprise. The way participants looked at the Agreement in large measure determined their response concerning the potential for social policy harmonization. For those who interpreted the Canada-U.S. Free Trade Agreement in strictly economic terms, problems of harmonization were related to the removal of trade barriers, economic specialization, and efficient resource allocation.

Cast in this light, the Agreement provided little evidence of formal restrictions on the right of Canadian governments to maintain and develop social programs.

To those who viewed CUSFTA as more than simply an economic matter, the central issue raised by harmonization was that of a perceived change in political values. In their eyes, the Agreement casts a shadow over Canada's strong tradition of public intervention and, in Leonard Shifrin's phrase, places us on a slippery slope leading toward a range of options,

virtually all of which are fraught with danger for the social policy sector.

The central question, which went largely unanswered, was to what extent other determinants of social policy harmonization (such as common values, common language, common institutions and common tax practices) would interact with the Agreement to intensify the pressure toward continental integration. To assume that such an interaction would not take place ignores the history of our two countries and the enormous influence the U.S. has wielded over Canadian life.

THE CANADA - U.S. FREE TRADE AGREEMENT

Trade Negotiations Office

Introduction

This paper outlines briefly certain elements of the Canada-U.S. Free Trade Agreement (CUSFTA) and reviews issues raised by critics regarding the effects of the Agreement on Canada's social programs.

To set the Agreement in context, we first should recognize that Canada is the only advanced industrial nation of at least 10 million people without an open market. The application of modern technology requires the specialization and scale made possible by a large market. CUSFTA overcomes this major Canadian deficiency. The multilateral forum remains the cornerstone of Canadian trade relations and we are fully committed to the Uruguay Round, but the pace of GATT negotiations and the complexities of accommodating nearly 100 countries with divergent interests makes it very difficult to meet all our trade objectives in that forum. Despite our efforts to increase exports to other countries, the United States now accounts for about 80 per cent of our goods exports. If the U.S. is going to become more protectionist, we had better not be on the outside looking in.

Canada took the initiative in negotiating a free trade agreement with the U.S. CUSFTA will govern a market of 270 million people that is expected to surpass a $200B exchange of goods and services in 1988. The Agreement will give us the ability to trade and invest in this vast market while remaining free to enjoy our essential political sovereignty. It will create a secure economic environment that will attract investment, lead to growth, and enable us to secure the standard of living and social programs we have come to regard as rights. We will retain the freedom to pursue our commitments to combating regional disparities and developing our unique cultural identity. A Winnipeg Free Press editorial last fall declared:

The real danger to social programs and cultural industries is not freer trade, but a stagnant or declining economy. Clinging to the status quo in a dangerously protectionist world would have risked economic stagnation or decline. Pursuing freer trade -- with the U.S. and the rest of the world -- offers the best hope for the economic growth which will give Canadians a better life economically, socially and culturally.

When this Agreement is fully implemented a decade from now, average Canadians will have more money in their pockets and a wider choice of competitively priced goods and services to spend it on. The Agreement does not threaten Canada's social programs. Social programs were never at issue. Elected governments will continue to determine social policy. CUSFTA will help promote economic growth to support these social programs.

Elements Of The Agreement

Since the release of the Elements of the Agreement last October and the full text of CUSFTA in December, a number of issues have been raised regarding its potential impact on a variety of government programs and various sectors of industry. A brief review of the elements of the Agreement that have been raised in the context of social issues, and a description of the rights and obligations flowing from these elements are required. In addition, where appropriate, examples of the Agreement's effect on particular situations are provided. For a more detailed understanding of the elements, the full text of the Agreement may be consulted. The key elements of the Agreement that give rise to concerns regarding social programs are dealt with in the following order: i) subsidies and dispute settlement; ii) cultural industries; iii) technical standards; iv) import restrictions; v) services; vi) procurement; and, vii) investment.

(i) Subsidies And Dispute Settlement (Chapter 19)

Although the negotiations attempted to develop a new set of rules governing the question of subsidies, none were in fact agreed to under CUSFTA. Both countries will attempt to develop and implement a substitute system of countervail and antidumping laws within seven years. In the meantime, a dispute settlement mechanism will guarantee the fair application of respective trade remedy laws. Either government may request a binational

panel to review final antidumping or countervail determinations. Panel decisions will be binding.

Clearly it would be preferable to have completed the work on new joint rules for subsidies. However, CUSFTA quite clearly provides for the continuation of all existing government support programs. It also institutes an improved method for ensuring that domestic trade remedy law is impartially applied.

Some commentators have queried whether Canadian social programs will be subject to U.S. countervail action. There are no circumstances under which any Canadian social programs (which are, after all, generally available) could be countervailed. One example raised by some critics of CUSFTA is medicare; on the other hand, critics have also suggested that Canadian industry will pressure governments to get rid of medicare because it constitutes an unfair competitive burden on Canadian industry. These two arguments are obviously inconsistent but have sometimes been pesented by the same commentators. Canada's health care system is a very effective way of providing health services to the population as a whole at a lower share of GNP than is the case for neighbours in the U.S.A. It is not at risk as a result of the Agreement.

The Unemployment Insurance program is another generally available program that would not be at issue. A specific case, the groundfish case, raised the question in the U.S. concerning special UI benefits for fishermen. The Americans argued it was a focused benefit for a small group, but the amount was so insignificant that the case was dropped. Other programs of widespread application (including retraining support, pensions, maternity benefits and so forth) are not in danger of countervailing action. The new dispute settlement mechanism also ensures that the binational panel (which includes Canadian appointees) will participate in the review of cases, and that there is no abuse of the trade remedy law in its application to specific cases. Canada therefore will have a more secure system through which cases will be heard.

Although the precise results of the forthcoming negotiations on the issue of subsidies are of course unknown, it is clear that generally available social programs will not be discussed by either side. Therefore social programs are not put at risk by the provisions on subsidies contained in CUSFTA as it stands, and they are not going to be vulnerable in the future.

(ii) Cultural Industries

Cultural industries, including broadcasting, publishing, sound recording and movies, are important in developing a sense of identity and communication among Canadians. The government recognizes the dominance of foreign, usually U.S. material in our media, and is determined that the free trade agreement should not reduce our ability to foster and continue to promote the development of Canadian cultural industries.

Article 2005 exempts cultural industries from the provisions of the Agreement, except for the following: the removal of tariffs; an undertaking with respect to paying fair open-market price for required divestitures of an indirect acquisition; the creation of right for "equitable and non-discriminatory remuneration" for retransmission of copyright holders' material; and, the removal of the requirement that periodicals be printed and typeset in Canada in order to benefit from income tax deductions for advertising placed in Canadian periodicals.

The definition of cultural industries set forth in Article 2012 is very comprehensive and covers all aspects of the production and distribution of cultural products. The United States has retained its existing ability to take measures of equivalent commercial effect if we fail to meet our obligation on these limited number of cultural measures. In all other respects, Canada is free to undertake measures in support of cultural industries and the U.S. is free to retaliate, but only in areas outside the Agreement.

(iii) Technical Standards (Chapters 6 and 7)

As signatories to the General Agreement on Tariffs and Trade (GATT) and its Technical Barriers to Trade (known as the GATT Standards Code), Canada and the United States recognize that technical standards could potentially be used to hamper international trade. Under the Canada-U.S. Free Trade Agreement, both countries agree to refrain from using technical standards and regulations for goods as barriers to trade. Standards and regulations will nevertheless continue to be allowed where their demonstrable purpose is to protect health and safety, the environment, national security, and consumer interests. Under the Agreement, Canada and the United States will work towards making national technical standards more compatible, and will encourage similar efforts at the

state, provincial and private levels. In fact, a great deal of compatibility in standards has already been accomplished.

(iv) Import and Export Restrictions (Chapter 4)

Both countries have agreed not to prohibit or restrict imports or exports of goods that are traded bilaterally, except under specifically defined circumstances. Canada and the United States have agreed to build on the provisions of GATT, which justify import and export control measures for certain reasons. Thus, for example, Canada will continue to apply appropriate measures to prohibit the importation of pornographic materials.

(v) Services (Chapter 14)

This chapter provides for the first time a general framework of rules for bilateral trade in services, which Canada and the United States have agreed to adopt in future laws and regulations. Both countries have undertaken an obligation, known as 'national treatment.' This requires them in any new laws and regulations to extend treatment to the other country's service providers that is no less favourable than the treatment accorded to their own providers. The two countries will accord the right of establishment, consistent with the Investment Chapter (see section vii below) and the right of commercial presence, that is, the right to be represented in each other's market.

The obligation to extend national treatment in no way impairs the government's ability to regulate a particular service sector. In the future, if Canada chooses to treat suppliers of services covered by the Agreement differently than does the United States, it is free to do so, as long as it does not discriminate between Canadian and U.S. firms. The national treatment obligation does not mean that treatment has to be the same in all respects, as long as the treatment is equivalent in effect. The Agreement does not require that regulations be harmonized or identical between the two countries; nor does it require governments to privatize services.

The chapter on services applies only to those services delivered by enterprises operating on a profit-making basis that are listed in the service sectors in annex 1408 to the chapter. Certain services are not covered by the services chapter because they are

not traded between the two countries as commercial services. For example, public administration, education, day care, and health and welfare are not covered services. Although the annex includes health care facilities, management services, and educational research services, these provisions apply solely to commercial services currently supplied on a limited basis by the private sector.

In general, government services -- including national defence, the justice system, education, health programs and hospitals -- are outside the scope of the services chapter. With respect to the accreditation and licensing of service providers who are covered by the Agreement (e.g., engineers and architects), provinces and states will continue to set the standards. New regulations must apply equally to Canadians and Americans. Americans wishing to do business in Canada will have to conform to our standards and regulations.

(vi) Procurement (Chapter 13)

The procurement undertakings are very modest and merely provide for a reduction in the existing threshold for procurements between Canada and the United States by the GATT procurement code. The code is limited to certain federal government entities who contract for goods or for services incidental to the purchase of those goods. Procurement by provincial governments and parapublic institutions is not affected, nor is the procurement of services. Thus, there is no obligation to provide contract opportunities to U.S. suppliers for the management of hospital services. For example, if hospitals wish to contract out services, they are free in their offer to tender to limit proposals to Canadian firms if they so choose.

(vii) Investment (Chapter 16)

The two governments agree, with certain exceptions, to provide national treatment in future to each other's investors. The Canadian threshold for review of U.S. direct acquisitions will be raised to Cdn $150 million by 1992. Existing laws, regulations and published policies restricting the right to invest in specific sectors are 'grandfathered' and remain in place. For services not covered by Chapter 14 (Services Chapter), there are no obligations regarding the conduct and operation of these businesses.

If any barriers to investment in specific sectors exist now -- such as, post-secondary institutions, day care facilities and medical laboratories -- they will continue to prevent U.S. companies from setting up or owning facilities in Canada. In addition, for services not covered by Chapter 14 (such as day care facilities) Canada has no obligation to provide national treatment for measures affecting the conduct or operation of that business. Therefore Canada would be free, for example, to prescribe regulations regarding the conduct and operation of day care facilities which would be more onerous on U.S.-owned firms than on Canadian-owned firms. We are also free to determine the type of day care program that we wish to see in Canada (e.g., not-for-profit, cooperative, government-run, or private-sector commercial service) and to adopt the policies necessary to put it into place.

Summary And Conclusions

This review of the major elements in the Agreement has outlined the obligations Canada and the United States will undertake in order to improve market access and increase trade between the two countries. An improved trading relationship will establish a large and secure market for Canadian goods and services. This in turn will increase investment in Canada and generate higher levels of income and wealth. The adjustments that must be made by Canadian industry in order to take advantage of this new U.S. market and deal with increased competition in Canada will be facilitated by the extensive range of adjustment and training programs offered through CEIC and various provincial training programs. Canadian business will be able to improve productivity as well as create more job opportunities and higher incomes. These advantages will help to ensure that Canada has the economic strength necessary to support its tradition of social programs, and that new policies and programs can continue to be developed in support of Canadians as Canada moves into the increasingly global marketplace.

DISCUSSANTS

Geoffrey Norquay

Before addressing some of the specific concerns raised by the social policy community about the Agreement itself, I want to make a plea for realism in assessing the impact of the Agreement on social programs. Many of the concerns raised in the social policy community appear to be based on the premise that Canada is about to move from a situation of no trade with the United States to total economic union with the United States. This is not the case. Roughly 80 per cent of Canada-U.S. trade is already unencumbered by tariff and non-tariff barriers. That has not prevented Canada from developing a health care system conceived, funded, administered and delivered in a totally different and clearly superior fashion to that of the United States. It has not prevented Canada from developing distinctive social service programs, as well as programs to promote our multicultural diversity and our linguistic duality.

From the outset of the negotiations, the government of Canada took the position that Canada's social programs were not on the table. That position was maintained to the conclusion of the negotiations. Furthermore, there is nothing in the Canada-U.S. Free Trade Agreement to limit the full exercise of sovereign power by the government of Canada or the provinces in the establishment and maintenance of social programs.

There are, of course, no absolute protections against U.S. claims that Canadian social programs constitute unfair subsidies. It is important to note, however, that such claims are entirely possible at the present time, in the absence of the Agreement. What is more significant is the virtual absence of trade actions involving social programs between the two countries. In all the years of trade between Canada and the United States, worth hundreds of billions of dollars, there has been only one situation in which a social program became the subject of a countervail action. That was in the 1985 countervailing duty case against the Canadian groundfish industry. That countervail claim was thrown out at the lowest level of adjudication within the U.S. Commerce Department.

The introduction to Chapter 14 of the Agreement says:

> With the exception of transportation, basic telecommunications (such as telephone services), doctors, dentists, lawyers, child care and government provided services (health, education and social services) most commercial services are covered.

This is the first line of defence against the Americanization of Canadian social programs. Health and social services are specifically exempted from the list of tradeable services. The second line of defence is Article 1601, paragraph 3, respecting investment. It specifically exempts from national treatment "investments related to the provision of services other than covered services." What this means is that the U.S. cannot use the investment provisions of the Agreement to extend access to health and social services otherwise precluded by Chapter 14.

With regard to management services of health care facilities such as nursing homes, they could be tendered commercially only in the event of a government decision to contract out to the private sector. There is no obligation on Canada to privatize management services under CUSFTA. Even if the government perceives it to be in the public interest to contract out certain aspects of health care facilities management, all government standards and criteria regarding quality of service would continue to apply. All management services that the government chooses not to contract out to the private sector come under the general category of government-provided services, and are therefore excluded.

In today's world, harmonization is a fact of life. Much has been made of the similarities between recent tax reform efforts in Canada and the United States. The plain fact is that all industrialized countries now face the same pressures to keep tax and fiscal policies roughly similar with each other. The mobility of capital, of job-creating investment, is a reality that all developed countries ignore at their peril. As a close neighbour to a major industrial power, Canada already lives with this reality daily. To the extent that the Agreement contributes to close economic ties between Canada and the United States, some increased harmonization may well result. But I would ask whether the difference between 80 per cent unencumbered trade and 95 per cent or 96 per cent is going to make that

much difference? Will Canadians in the future fear domination by the United States? Some probably will, just as they have in the past, but that was a concern long before anyone thought of a free trade agreement.

Barbara Arneil

The effects of CUSFTA on social policy can be categorized in two ways. The first is the impact of specific provisions within the Agreement itself. The second is how the larger dynamic forces unleashed by the Agreement will affect our future choices.

The overarching principle of the chapter on services is "national treatment." The implications of national treatment are that no measure which would either discriminate against an American firm or distort trade can be brought in by a federal government. The government argues that social services are not included in the deal and never will be. Clearly under the annexes attached to this chapter, health services are included. In fact, everything from hospitals to nursing care to medical laboratories is covered. Moreover, Article 1405 allows for the inclusion of further services. Thus, any services either currently excluded or not explicitly referred to could be included. Under Article 2010 of the Agreement, any future Canadian government that wants to create a new crown corporation or expand the scope of an existing one will have to notify and consult the American government, and then ensure that the crown corporation was non-discriminatory and "disciplined." This has implications for both provincial and federal governments who may wish to provide services on a universal basis. Also, the agriculture section virtually concedes that certain regional development programs are no more than subsidies needing to be disciplined.

One of the long-term future implications of the Agreement is an overwhelming pressure for governments and private industries to harmonize. As Canadian companies are brought into direct competition with their American counterparts, there will be increasing demand on the government to bring the fiscal framework, corporate taxes, and regulatory environment into line with that of the Americans. The Conference Board of Canada predicts that the federal deficit will increase as a result of the Agreement; lower revenues will lead to increased demand to cut spending on social programs. Add to this dynamic mix of political and economic forces

an enormous cost increase to the health system resulting from the pharmaceutical bill (included in the first draft of the Agreement and clearly an item on the U.S. agenda in these talks) and one can envision the decision to start chipping away at our health care system through, for example, the introduction of user fees by provincial governments. It is this largely incremental and inconspicuous weakening of our social programs which will result from this Agreement that critics fear, not the elimination of social programs but their erosion.

Pressure will also be brought to bear on Canadian companies who must compete with American firms in the South. Manufacturers in the northern states have already felt 'the heat' and taken the losses. Consider that employment in the manufacturing sector in the states of Michigan, New York and Ohio decreased between 1973 and 1980 by 17 per cent, 10 per cent and 11 per cent respectively. Compare these figures with those of Texas and California, where manufacturing employment increased by 31 per cent and 21 per cent respectively. Lower labour costs, fewer unions and fewer benefits all contribute to this trend in the southern states and draw business away from the north. Consider also that right-to- work (anti-union) legislation exists in twenty southern states. While employment over ten years has increased by 3.5 per cent in right-to-work states, states without right-to-work legislation have witnessed a 13.4 per cent decrease in employment.

One of the areas that has received the least consideration is what will happen to the federal government's commitments to the aboriginal people under free trade. The head of the Dene Nation recently warned members of the parliamentary committee that this Agreement could have implications for all native people. He made several points. First, the aboriginal people were never consulted during the negotiations. Second, many of his people had no need for access to the U.S. market. Third, he wondered what impact the Agreement would have on native land claims, particularly on negotiations over resource revenue sharing arrangements. Would such arrangements be considered a subsidy? What effect would the negotiations with Americans on subsidies have on the Northern Economic Development Programs? Finally, he queried whether affirmative action programs for natives would be allowable under national treatment for services.

The Agreement has profound implications for Canada's social policy over the long term. The resulting

pressures will be felt by Canada's business community and governments at all levels. CUSFTA will not strike at the heart of our commitment to universal and accessible social programs, but it will eat away at the edges, gradually eroding the social contract we now hold so dear.

Bruce Campbell

It is hard to accept the assertion of the Trade Negotiations Office (TNO) that the Agreement safeguards the public welfare. Perhaps the government's claim would have been more believable if the Agreement had contained a clause exempting social programs (similar to the cultural industries' exemption under Article 2005). Of course, this would have been unacceptable to the Americans because the issue is central to their unfair subsidy claims.

The TNO paper is less than forthright when it claims that government-provided services such as health care are not part of this Agreement. In fact the management of all hospitals and most social services is covered in the chapter on services (Annex 1408). The list includes all general hospitals, psychiatric and children's hospitals, and community health clinics. Governments favouring the privatization of these services -- such as the current one -- apply pressure by cutting budgets and forcing institutions to cut costs. This is already happening. Three hospitals in Ontario have opted for management by U.S. corporations.

It is one thing for a government to undermine the quality of health care via its policy of privatization. It is quite another to allow U.S. companies to participate on an equal footing, and to enshrine these rights in an international agreement. A future government that wished to restore the quality of health care would find costs prohibitively expensive. It would have to provide U.S. companies "prompt adequate and effective compensation at fair market value" for measures considered to be "tantamount to expropriation" (Article 1605); and it would basically have to get permission from the United States government (Article 2010) as to the amount.

Regarding social services, I would like to make just three points. First, while child care is not currently on the list of covered services, it might well be in future as the Agreement expressly provides for additions

to the list. Secondly, a U.S. day care firm could complain that it is being discriminated against contrary to the national treatment clause (Article 1602) and cause the matter to be dealt with through the dispute settlement process (Article 2011). Thirdly, a future government that wanted to institute a national public day care program would face the same financial barriers mentioned earlier.

The most important impact that this Agreement will have on Canada's social programs is indirect. The logic of the resulting harmonization process is that intense pressure will be brought to bear from within the Canadian business community to reduce the Canadian social contract toward the lower social contract prevailing in the American marketplace. On this matter, the TNO paper is silent. The United States social contract is generally inferior, but much more so in the southern states. In addition, the United States has "back doors" that are becoming an important part of the unified North American market -- the Maquilidora free trade zones along the border with Mexico and Puerto Rico. These regions give corporations powerful levers to depress the social contract. Relocation, or just the threat of relocation is sufficient to pit one group of workers against another, one community against another, in the scramble to offer concessions.

Leonard Shifrin

The real question of this debate is not whether the free trade agreement will create a few more jobs in this country than it destroys, or a few less. Nor is the question whether Canadian consumers are going to be a few dollars better off or not. The real question is "Will Canada be able to maintain its social democratic tradition if tied more closely to the United States?" Or, to put it another way, are we all eventually going to find ourselves living in the U.S. without even having gotten warmer winters in the bargain? Those who would have us believe that such fears are groundless point to free trade experiences elsewhere in the world as evidence that no such fate lies in wait for us. These reassuring precedents are not so reassuring because they are non-analogous in very crucial ways. There is no precedent for two countries of such disparate size, with a common language but very different social traditions,entering into such an arrangement.

There are two categories of danger for Canadian

social programs in such a venture. One is that certain of these programs, particularly those providing income or income-in-kind, could be regarded by the Americans as subsidies to business in this country, leading to the imposition of countervailing duties. The other is that some social measures, particularly labour standards of various sorts, will be eroded as a result of Canadian business insisting that it cannot meet American competition if its costs are higher than those south of the border.

It may seem inconsistent that Canadian business groups so often denounce as a burden the very programs that American interests see as a subsidy to companies in this country, but it really isn't. The Canadian companies that object to being required to contribute to maternity benefits through unemployment insurance, for instance, are typically small, non-unionized employers who wouldn't provide such benefits on their own. The American companies who see the measure as a subsidy to their Canadian competitors are the large, unionized firms, which are obliged to provide these benefits by their union contracts.

The TNO paper glosses over the failure of Simon Reisman and Peter Murphy, in their sixteen months of negotiations, to reach agreement on the subsidy code that would protect Canadian social programs from being ruled 'subsidies' with countervailing duties imposed. There is nothing to worry about, the paper assures us. Let me give you a quote from Simon Reisman last November, describing the negotiations. "Powerful American interests had targeted our social, cultural and regional programs for elimination as their price for an agreement," he told the University of Manitoba Faculty of Management. "The Americans wanted very tough rules on subsidies for us, but not for them."

Under such circumstances, one would expect any reasonably prudent government to insist that the subsidy question had to be settled before any agreement could be entered into. But this government didn't. The result is that we have painted ourselves into a heads-they-win-tails-we-lose situation under the free trade agreement. If Canadian companies are losing the contest, they will insist that they can't carry the burden of our higher minimum wage requirements and other more rigorous labour standards. If Canadian companies are winning, then the Americans will insist it is because of the subsidies provided by lower employer pension costs, smaller health insurance contributions,

and so on, and impose countervail.

If the binational dispute settlement panel is supposed to be a great defence against American outrageousness, just take a look at a map of North America. Both the Alaska panhandle that cuts off the Yukon and northern B.C. from access to the sea, and the Maine wedge that sticks up into where the rest of New Brunswick should be were the products of U.S. big-stick tactics on binational panels. The Canada-U.S. Free Trade Agreement puts us on a slippery slope toward a range of possible scenarios, virtually all of which are fraught with danger for the social policy sector. It is a leap of faith that no one concerned with the future of social programs in this country should be willing to make.

HARMONIZATION OF SOCIAL PROGRAMS UNDER FREE TRADE

Derek Hum

Prime Minister Mulroney and President Reagan agreed in Quebec City on March 18, 1985 to establish a new trade agreement between Canada and the United States. This agreement would "reduce and eliminate existing barriers to trade in order to secure and facilitate trade and investment flows." After much negotiation, Canada and the United States signed an accord on October 4, 1987, setting out the elements of a bilateral trade agreement. Two months later, Canada tabled the Canada-United States Free Trade Agreement (CUSFTA) in the House of Commons.

This Agreement is extremely broad in scope. Nonetheless, it is consistent with Article XXIV of the General Agreement on Tariffs and Trade (GATT), which provides the framework in international law for free trade agreements. Furthermore, the preamble to CUSFTA establishes immediately that this is a trade agreement. It is not meant to deny either party the right to preserve public welfare. Indeed, Canada claims that CUSFTA, once in force, will lead to a richer nation, which in turn will allow the government "to stimulate economic development in Canada's poorer regions and strengthen social programs for all Canadians."[1]

Both during and after the negotiation of CUSFTA, misgivings were expressed concerning the sanctity of Canada's social programs. On the one hand, Trade Ambassador Simon Reisman and others repeatedly asserted that social programs were not "on the table," a position seemingly endorsed by the U.S. envoy.[2] On the other hand, the Canadian Labour Congress opposes free trade, in part on the grounds that it would destroy our capacity to maintain universal social programs. Similarly, the Council of Canadians warns that free trade may lead to such a matching of Canadian policies

with American policies that Canada's political sovereignty ultimately could be emasculated. Glenn Drover observed that positions taken by both sides concerning the question of free trade's impact on social policy, "while passionately put, have been unaccompanied by systematic investigation."[3]

It is not a new notion that a free trade agreement with the United States will inevitably require Canada to implement economic and social policies identical or substantially similar to those of the U.S. There is a substantial body of literature on the subject of national policy harmonization that dates from the late sixties, and was motivated by the actual formation in Europe of various trading bloc arrangements. However, much of that analysis focused upon the harmonization of fiscal, monetary and balance of payments policies, to the relative neglect of social policies. Furthermore, the discussion took place in the context of a particular set of institutions and customary policy practices.

This paper addresses a more narrow formulation of the question: will CUSFTA lead to pressure to harmonize Canada's social policies with those of the United States? The questions concerning harmonization raised in the late sixties are, accordingly, re-examined in light of the details of this specific North American agreement, taking into account certain political and economic trends in Canada, including the Meech Lake Accord and the need for tax reform.

The late Harry Johnson provides a useful taxonomy of harmonization policies, distinguishing between structural and balance of payment policies. Structural policies refer to the levels and types of taxes and government expenditures, the regulation of competition, and the like. Balance of payments policies refer to the choice of instruments used to achieve external equilibrium and includes such measures as the exchange rate, capital controls, and so forth. Social security programs are therefore considered to be a sub-class of structural economic policies. As to the definition of harmonization itself, Johnson offers the following:

> In the context of a free trade area... the harmonization issue with respect to structure appears partly as an obligation on participants not to use other policies to nullify the economic consequences of the elimination of trade barriers, and partly, and more importantly, as a question of

> what changes or alignments to make in other policies in order to facilitate the desired efficiency-increasing results of free trade or to augment those results beyond what they would otherwise be.[4]

Johnson's taxonomy is not the only one available. R. Lipsey and M. Smith distinguish between broad-based versus sector-specific policies, and between post-agreement versus agreement-directed pressures to harmonize.[5] For present purposes, Johnson's categorization seems better for two reasons. First, it clearly identifies and locates social programs within the class of structural policies, allowing us to focus upon tax, transfer and expenditure measures. Second, it serves to separate the issue of harmonizing social programs from discussions of the exchange rate. This is an important distinction because the view, in some quarters, seems to be that all will be fine if exchange rates are flexible. For example, D.J.S. Brean writes:

> ... a higher social security tax for workers' compensation, or differences in comprehensive unemployment insurance programs, or similar general differences in fiscal systems -- either on the tax or the expenditure side -- cannot create permanent competitive advantages or disadvantages in trade **if exchange rates are flexible** [emphasis added].[6]

Brean's strong statement in regards to flexible exchange rates stems from a concern about the allocative efficiency of a free trade agreement. It ignores the point that social policies are not directed first and foremost towards allocative efficiency.

It is important at this juncture to clarify terms. What is meant by social policy are those programs transferring cash or in-kind goods to individuals or regions. Canadian programs such as family allowances, old age security, public pensions (CPP/QPP), hospital and medicare, post-secondary education transfers, and the like are included, as is almost the entire range of programs delivered through the Canada Assistance Plan. Even equalization transfers might be included. The touchstone of social policy is the redistributive function, rather than the allocative function. This may be labelled 'the social welfare perspective.'[7]

A second category of social programs includes the various forms of social insurance. Unemployment insurance and workers' compensation are perhaps the best known examples. Social insurance programs represent measures providing individual economic security through the public sector, rather than through the private market. These measures are not necessarily or primarily designed to redistribute wealth from the rich to the poor. In many instances they are introduced to correct what economists term 'market failure.'

Social policy, in sum, comprises those programs whose objective is either redistribution or the correction of market failure. Using this definition, the question of whether a free trade agreement will bring about the harmonization of social programs is revealed at its core. A free trade agreement signifies that competitive market forces will be allowed to determine the allocative decisions of partner nations. The market is indifferent both to the resulting distribution of income and jobs, and to the risks that individuals will have to bear. On the other hand, the deliberate intent of social programs is to the redistribution of income and the safeguarding of citizens from various contingencies. Hence social policy must, to some extent, eschew the market. The question of whether CUSFTA requires the harmonization of social programs between Canada and the United States is made all the more compelling by the ironic fact that social policy in North America can often be more laissez-faire than economic policy.[8]

In considering the possible effects of CUSFTA, economic theory, historical experience and current trends suggest two lessons. First, the extensive harmonization of social policies as a result of CUSFTA is unnecessary. To this end, the next section summarizes the public fears and the economists' conventional wisdom on the question. This is followed by a more specific discussion of the CUSFTA and what it implies for Canada's contemplated reform of its tax system as well as future exchange rate stance. Second, while many of Canada's social programs or policy directions are likely immune from harmonization pressures, the area of income maintenance to working individuals and the practice of regional industrial subsidies are quite vulnerable, and made even more difficult to promote as a result of the Meech Lake Accord. This argument, and some concluding observations, comprise the last two sections of this paper.

Common Fears and Conventional Wisdom

Canada entered CUSFTA with the expectation of gaining enhanced economic benefits and security of access to the United States, a market many times larger than that of Canada. The U.S. is the country with whom Canada now conducts most of its trade. The relative size of the two countries, as well as the already significant amount of trade, condition Canadian perceptions on the harmonization issue. The idea that Canada's social programs are sufficiently distinct from, and more extensive and generous than those available to Americans raises for Canadians the question of economic policy harmonization. Since Canada is so much smaller than the United States, harmonization will mean altering Canadian social programs to conform to American ones, implying a tremendous loss of political sovereignty. Furthermore, CUSFTA represents the transformation of imagined fears into a real and apprehended danger.

The extent of trade between the two countries prior to CUSFTA is relevant here, as is the fact that current levels of tariff protection are not especially prohibitive. Accordingly, the issue is not whether trade <u>per se</u> leads to the necessity or desirability of policy harmonization, but rather to what degree the extra trade induced by CUSFTA lends itself to additional pressure for policy harmonization. There can be no doubt that an explicitly formal agreement such as CUSFTA, with its institutional and procedural arrangements, constitutes a greater restraining force on policy than does the mere volume of trade itself.

The conventional wisdom in economic literature is that the need for harmonization beyond that already required of countries extensively engaged in trade is slight.[9] The basis of this position, initially developed in the late sixties, rests on several considerations. These include the distinction between a free trade arrangement and other forms of economic integration such as a customs union, a common market or a political union; the distinction between comparative advantage versus absolute advantage in explaining trade patterns; and, the understanding of macro stabilization policies and their relationship to the exchange rate.

It is useful to recall that the harmonization issue first arose in Europe, where countries contemplated an economic and political integration greatly in excess of that implied by a mere free trade area. Briefly, a free trade agreement involves the elimination of tariff and

non-tariff barriers between trading partners. Each country is still free to set its commercial policies with respect to non-partners, and there is no requirement to foster free mobility of labour and capital within the free trade area. Consequently, there is no need to harmonize macro stabilization policies, immigration policies, or even personal income taxation policies and the like. Where explicitly acknowledged at all, social programs are not a problem. The crux of this argument lies in the view that a free trade agreement is concluded chiefly to maximize the consumption of private goods by both trading partners, and that the unfettered market is the best mechanism to allocate resources, signal specialization lines, and so forth. With this objective, economic theory explains that in a non-tariff-ridden world, it is comparative rather than absolute advantage that determines trade.

The 'ignorance' of 'practical' people, as Johnson[10] phrases it, is responsible for the belief that the factor determining whether or not Canadian-produced widgets are exported is their cost relative to that of producing similar widgets in the United States. Hence, the argument goes, if Canadian social programs increase Canadian costs overall, then Canadians must align their social programs to avoid this absolute cost disadvantage. But as students of international trade know, it is comparative costs that are important. Put another way, it is not the absolute cost of Canadian widgets compared to American widgets that is important; rather, it is the cost of Canadian widgets compared to the cost of other Canadian-produced goods that matters.

Many economic students have struggled to master the subtleties of comparative advantage theory, known since Ricardo. If this is thought to be the litmus test of functional literacy in economics, then perhaps Johnson is correct in claiming widespread public ignorance. Nonetheless, from the perspective of political economy, it is open to question whether real-world trade determinants conform to the economic theory of comparative advantage. Further, whether or not businessmen and politicians get failing grades in economics, the lobby for social policy harmonization may not be any less strong or successful despite being grounded in 'mistaken' beliefs. The capacity of the economics profession to enlighten the general population on the finer points of comparative advantage theory is likely to win even less success than have teachings about the merits of an occasional unbalanced budget. In short, pleas for the harmonization of Canada's social

programs with American practice can be expected to materialize following the implementation of CUSFTA.

The recent discussions of policy harmonization and free trade differ from the debate conducted in the late sixties. That earlier discussion paid little or no attention to social programs, but considered in detail the question of balance of payment policies. The observations of the sixties took place against the backdrop of the European Economic Community and its commitment to fixed exchange rates. Understandably, much concern was expressed about the need to harmonize fiscal and monetary policies in order to stabilize national economies and clear external balances. The lessons of that analysis are still valid. P. Wonnacott made it quite clear that "fiscal policy rises in relative importance as the commitment to fixed exchange rates grows."[11] Johnson identified the root cause of harmonization pressures: "It is the fixed exchange rate system, essentially, and not the free trade arrangement, that raises the issue of harmonization of balance of payments policy among members of a free trade area."[12] It is now commonplace in modern macroeconomic texts to teach that adherence to a fixed exchange rate obliges a country to give up control of its money supply.[13] In the context of CUSFTA, this means that the twin objectives of efficient, long-run allocation of resources and maximum independence for monetary policy to pursue domestic targets are best achieved by flexible exchange rates. In other words CUSFTA implies, at the very least, commitment to a semi-clean float of the exchange rate. Given the current Canadian stance on exchange rate policy, CUSFTA is unlikely to raise difficulties on this point.

Still, the beneficial consequences of a flexible exchange rate may well be overstated by modern commentators. For example, Lipsey and Smith suggest that a free trade agreement between Canada and the United States would not necessitate increased policy harmonization because of the "role of the exchange rate as an overall adjustment mechanism."[14] Brean would apparently apply this argument to social policy as well.[15]

The Lipsey-Smith position, while fundamentally correct, treats Canada as a homogeneous entity abstracted from the wide variation in economic activity that, in fact, exists among Canada's provinces and regions. Within this context, the exchange rate cannot be relied upon to achieve regional balance or equity.

From the standpoint of stabilization objectives such as reducing unemployment in various parts of the country, Canada is not, in the jargon of economics, an optimum currency area. The Brean position also suggests that social programs are broad-based policies. They affect absolute but not comparative cost, and therefore do not distort trade. Hence, social programs that merely increase Canadian absolute production costs can be accommodated by an appropriate movement of the exchange rate. This line of reasoning depends on the critical premise that social programs affect costs, if at all, uniformly. But in many cases social programs deliberately set out to achieve a non-uniform result, both in terms of financing and choosing individual and regional targets for benefits. To the extent that this happens, there will be distortions that are not compensated for by the exchange rate. Again, in the jargon of economics, social policy-induced disturbances of absolute advantage also alter comparative advantage.

To summarize, fear exists among the public that a free trade agreement between Canada and the United States will oblige Canada to alter its economic and social programs to match American policy. Conventional economic wisdom suggests that harmonization pressures are minor. The debate in the sixties centred on fixed exchange rates, while present-day thinking would concede certain advantages to flexible rates. Still, the role claimed for flexible exchange rates may be exaggerated with respect to social policies.

Social Policy and CUSFTA: Selected Comments

The Canada-U.S. Free Trade Agreement is a complex document. There are eight parts, each part has several chapters, and chapters are further divided into articles. The preamble and Part One establish that this trade agreement is consistent with GATT. Parts Two, Three, Four and Seven deal with trade in goods, government procurement, and services, broadly interpreted. Parts Five, Six and Eight deal with institutional and procedural matters, such as dispute settlement provisions, timetables and the like.

Since our concern is the possible harmonization of social programs as a result of the free trade agreement, we shall concentrate on the general approach implied by the Agreement. However, several observations are worth noting in light of the literature on harmonization that developed in the sixties. First, the customary position on government procurement was one of exclusion; that is,

the practice of permitting governments at all levels to discriminate in favour of national and resident producers. CUSFTA appears to go further than perhaps is necessary by increasing the amount of procurement open for competition between U.S. and Canadian suppliers in each others' market. Specifically, CUSFTA lowers the threshold from $238,000 to $33,000 for covered government purchases not excluded for national security reasons. However, the benefits may be slight.[16] Harmonization is unlikely to have a major impact on social programs on this account.

CUSFTA is concerned with the free movement of goods and services. Part Two sets out the requirements for eliminating tariffs, the rules of origin provisions, border measures, and elaborates the obligation of 'national treatment.' Because CUSFTA establishes a free trade area rather than a customs union, Canada and the United States remain free to independently determine tariff levels for outsiders. However, in order to avoid trade deflection (third country goods entering the free trade area via the country with the lower tariff structure), rules of origin and other border measures are necessary. Within this setting, the harmonization issue becomes to what extent Canada and the United States will have to adopt roughly similar border tax measures in order not to undo the trade objectives of CUSFTA.

The harmonization issue involves several questions, including a choice of either the origin or the destination principle for border adjustments; the mix between direct taxes (say, income tax) and indirect taxes (say, sales taxes); and, whether tax rates and the like must be uniform. These topics are exceedingly technical and can only be touched upon here.

The origin versus destination principle decides whether taxes are levied at the point of production (origin) or consumption (destination). A system based upon the destination principle would therefore not tax exports. This could have a bearing on social programs and trade measures. For example, imagine that destination-based tax revenues were used to finance government-provided local public goods or directly consumable benefits to individuals. This arrangement might be judged appropriate on the grounds that the country whose citizens receive the social benefits (say, for instance, local libraries and income assistance) are in fact the ones actually paying the taxes. On the other hand, if destination-based taxes were employed to reduce

production costs of tradeable goods, rather than spent on social programs, then such indirect taxes are de facto subsidies to exports. In sum, the question of whether the destination versus origin basis for levying taxes is trade-distorting, or whether it facilitates social programs depends on the nature of the expenditures.

There are, obviously, many additional considerations in deciding upon reform of indirect taxes in Canada, including administrative ease, revenue growth, tax evasion and the like. It may well be the case that the second stage of tax reform in Canada -- namely the replacement of the manufacturer sales tax -- is necessary for other reasons. In the present context, CUSFTA might tip the balance toward some sort of single rate, value-added tax (VAT) and the destination principle.[17]

The above remarks also apply to border tax adjustments, duty drawbacks and remissions, etc. An extreme form of the argument would extend the need for harmonization to all indirect levies. There is also the question of direct taxes, such as the personal income tax. The value of a tax like VAT must be assessed in conjunction with the direct tax system.[18]

Two observations should be kept in mind from our discussion of indirect taxes and the destination principle. First, it is now well accepted that the correct approach must combine taxes and expenditures. In other words, fiscal harmonization must take into account not only taxes (revenue side) but also government expenditures (benefits side). The concern is with what public finance specialists term 'net fiscal burdens' or 'fiscal residua' -- in short, the difference between taxes paid and benefits received. Second, the appropriateness of the destination basis for structuring border taxes is dependent upon accepting the benefit principle of taxation. The income tax is based upon the origin principle and typically considers ability to pay.

The income tax is a focus for fiscal harmonization under any free trade arrangement, for a variety of reasons. First, it can be argued that fiscal neutrality requires substantially similar, if not uniform tax structures, since divergences would induce distortions. These distortions include labour migration resulting from differences in personal income tax rates, and capital movements arising from differing corporate

taxation rates. Furthermore, evidence is available that individuals do move in part as a response to fiscal measures.[19] It also has been suggested that some social expenditures impede mobility, thereby lessening allocative efficiency gains -- for example, generous Unemployment Insurance payments impede the migration of surplus workers to parts of the country where there are jobs. These arguments, when addressed to social programs in particular, are irrelevant and fallacious. As noted, this view mistakes a free trade arrangement for something requiring greater integration -- CUSFTA is not intended to go that far. Capital and labour mobility between Canada and the United States takes place in spite of different fiscal regimes.

The precise point to social program expenditures typically is lost in the argument about harmonizing fiscal conditions. The salient fact is that social programs often have as their explicit objective the redistribution of income. Tax and transfer policies accomplish this to some extent through the personal income tax system. The questions of production incentives and geographical incidence are beside the point. Wonnacott, in a slightly different context, has this to say about the necessity of harmonizing income taxes to secure the advantages of a free trade agreement:

> ...objections to income tax systems on the grounds that they reduce movement to geographical areas of higher wages is... one of the subcases of the general proposition that income taxes discourage movement to higher-paying jobs, wherever they are located... This proposition holds whether labour is homogeneous or not, provided there is some substitutability among factors in the productive process. If incentive levels are to be restored... it would seem logical to abolish income taxes and put taxation on a benefit basis. However, if redistribution of income is accepted as an important function of the fiscal system, this option is no longer open.[20]

There is, then, no real need to harmonize with respect to the personal income tax system. Not only is the requirement absent in a free trade arrangement, it also is not relevant with respect to expenditure items earmarked for social policy. This is simply because a major objective (but not the only objective) of social

programs is to effect redistribution. It requires a very long stretch to reach the position where the consequences of social programs are so trade distorting as to undermine CUSFTA, although one exception is discussed below.

Two other provisions of CUSFTA deserve comment. The first is the 'national treatment' philosophy expressed in various sections of CUSFTA. National treatment means that goods and services, once imported, cannot be subject to further discrimination. Otherwise internal measures merely replace trade barriers. Its practical effects are to require that internal taxes (such as sales or excise taxes) be no higher on imported goods than on domestic goods; and that technical specifications (such as health and safety standards) cannot be more stringent for imported goods than for domestic goods. Canada can continue to require bilingual labelling, metric measurement, and regulation of items such as handguns, provided only that such rules apply to Canadian goods as well. National treatment does not mean that imported goods must be treated in the same fashion as they are in their country of origin. But while this is the general approach (Part Two, Chapters 5 and 6), there are also provisions to allow flexibility in national treatment, so long as the treatment is 'equivalent' (Article 1602). More pertinent to social program providers is Article 1402, which exempts childcare and government-provided services such as health, education and social services from the national treatment obligation. How telling these provisions will be for the long-run independence of Canadian social policy is an open question. CUSFTA does not contain strong measures to make Canadian social policy conform to American practice. However, there appear to be some restrictions on the future development of social policy, and possibly one contentious area. These will be pointed out in the next section.

Non-alarmist Reservations

Conventional wisdom suggests two conclusions. The first is that extensive harmonization of economic structural policies is unnecessary. The second is that macro-stabilization questions need not pose difficulties if exchange rates are flexible. But to what extent are these conclusions valid for social policy? This section suggests that social program areas such as health, post-secondary education, old age security and, to some extent, unemployment insurance are not generally vulnerable. On the other hand, certain income

maintenance trends, and regional and industrial development programs are problematic for CUSFTA.

Consider the proposition that flexible exchange rates eliminate the need to harmonize adjustment policies. The standard argument runs as follows: non-wage compensation measures such as pension benefits, social security, health care and unemployment insurance affect only absolute cost levels. Differences in absolute costs do not distort trade. Therefore, there is no need to harmonize social programs because each country's sovereign decision to alter social benefits will be fully offset by a movement of the exchange rate. Canada need have only the continuing resolve to maintain a flexible exchange rate.

There are two serious qualifications to this position. First, this argument views Canada as an undifferentiated and uniform national entity, while in fact it is a collection of regional economic units having widely different structures and degrees of labour mobility. Indeed, labour may not be as mobile from region to region within Canada as it is between parts of Canada and the United States. Consequently, Canada and the United States are not optimum currency areas. A single currency area is optimal insofar as factor mobility within the area is reasonably high.[21] To illustrate, if Quebec workers are reluctant to move to British Columbia but Ontarians are willing to migrate to the United States, then the Canadian exchange rate will prove too crude an instrument to combat national unemployment.

Implicit in all this is the assumption that Canada has a collective desire for regional balance. If this is the case, then Canada may also want to have a regionally differentiated fiscal policy. In any case, individual provinces will certainly seek to confer advantages to production within their own boundaries. This raises a crucial question. Will regional development programs be permitted under CUSFTA? It is simply not known at this point. Precise definitions of what constitutes government subsidies and anti-dumping provisions made under CUSFTA are to be worked out over the next five to seven years (Part 6, Chapter 19). Nonetheless, the United States has not been reluctant to employ countervail tactics in order to achieve its interpretation of the 'level playing field.' The Michelin Tire decision in 1973 is particularly illuminating. The United States found Canadian regional development grants to be an unfair export subsidy,

justifying countervailing U.S. duties. But as Brean noted:

> A world scale tire manufacturing facility cannot be located in a region such as Eastern Canada without most of its output being exported... For Michelin, the subsidy arguably was an offset to a natural cost disadvantage of locating in a particular region and was thus equivalent to a rebate of a location tax on exports... So long as the United States... consider[s] subsidies to export-oriented firms and industries to be selective export subsidies, the system is obviously heavily biased against... Canada, with [its] smaller domestic market.[22]

To those who argue that CUSFTA represents future arrangements rather than past practice, it must be said that the new rules have yet to be specified, the bilateral panel process has yet to be tried, and the term 'subsidy' has yet to be defined.

There is a second qualification concerning the proposition that flexible exchange rates will correct Canada-United States absolute cost differences arising from social benefits. It focuses on the assumption that social programs are necessarily, or even typically national. In fact, even programs such as unemployment insurance are national only in coverage. With regionally differentiated benefit structures or delivery provisions (typified by the wide variety of CAP programs) social programs can indeed alter comparative advantage, and in theory distort trade. The amount of trade distortion, real or imagined, is a highly contentious subject. This question is perhaps best considered in terms of individual income security measures. But first, it is useful to recall the raison d'être of a social program.

The economic motivation for a bilateral free trade arrangement is to raise the consumption of private goods and services in both countries, and to bring about an efficient allocation of resources in the free trade area. Accordingly, harmonization of policies other than tariff and non-tariff barriers may be necessary to secure these economic benefits. Taxes and expenditures that achieve the same effects as tariffs represent covert protectionism, and hence distort trade. On the other hand, social policies are not primarily concerned

with allocative efficiency, but rather with distributive questions. The decision to alter the distribution of individual incomes through progressive taxation or income transfers is both an exercise of sovereignty and a deliberate decision to override market mechanisms. Social policy also seeks to alter the mix of public and private goods, or perhaps simply to alter consumption patterns in the name of 'peace, order and good government' as in Meade's oft-quoted example of taxing alcohol and subsidizing milk.

That said, the difficulty lies in determining to what extent tax and transfer programs are covert protectionism substituting for the now-prohibited tariff measures, and therefore distorting of allocative efficiency. This must be distinguished from efforts designed to enhance citizen well-being and redistribute income, which therefore trade-distort incidentally, if at all. The standard view is that social programs, as a class, represent broad-based policies "not aimed at distorting trade and that any such effects are incidental."[23] While some programs (e.g., unemployment insurance) may have features that could be construed as trade-distorting, such as paying additional benefits to specific regions (those with high unemployment) or to special groups (east coast fishermen), these can be handled on a case-by-case basis by applying a 'specific test' and 'significant injury' rule. In other words, does the program in question achieve protective goals? This might be termed the 'pith and substance' criterion. And is the trade distortion sufficiently large to cause significant injury to the free trade partner?

Two further considerations are worth noting. First, taxes and subsidies perceived as distorting factor markets are more likely to raise objections than are those affecting final consumption demand. For example, a social policy that taxes liquor and subsidizes milk in the name of promoting sobriety and nutrition is probably less objectionable than are grants to distilleries and concessions to dairy operations. Second, taxes and transfers made to productive factors that are incapable of much supply response (in other words, inelastic) are also likely unobjectionable. In sum, social programs that deliver benefits to Canadians as consumers rather than as producers, that confer benefits on a universal rather than a targeted basis, and that have little supply response are probably immune from criticism. On this basis, social programs, including old age security (OAS), Canada Pension Plan (CPP), guaranteed income supplements (GIS), family allowances (FA), medicare and

post-secondary education (PSE) assistance should be easy to defend on merit. These programs are broadly based, universal (in the sense of not requiring an incomes-test, except for GIS) and they do not affect Canadians as labour factors of production. The OAS, CPP and GIS are directed toward people not in the labour market, as are PSE and FA. It is also hard to take seriously the assertion that there is a strong link between the provision of public medicare and the supply responses made by labour. On the other hand, depending upon program design, unemployment insurance and workers' compensation are more contentious.

The most troublesome policy area is likely to be that of individual income maintenance programs, especially those designed with the working poor in mind. It is well recognized that Canada's social security system does not pay adequate attention to this group.[24] Furthermore, the development and discussion of income maintenance policy in Canada has always been conditioned heavily by the relationship between income transfers to the working poor and work disincentives (labour supply response). This was true of the Social Security Review and the various episodes surrounding the possibility of a guaranteed income for Canadians.[25] Finally, unit labour costs constitute the major portion (roughly three-quarters) of average unit costs of production.

Recent tax reform measures represent a step that prepares for a negative income tax in Canada. The substitution of tax credits (some refundable) for exemptions is significant. It is easy to show that a system of refundable, income-tested tax credits is formally identical with the classical notion of a negative income tax.[26] Furthermore, the OAS/CPP/GIS combination effectively constitutes a guaranteed income program, albeit with eligibility restricted to those over sixty-five years of age. Finally, some provinces at various times (for example, Quebec) have introduced earning supplementation programs in order to aid low-income workers.

The worrisome issue, politically and economically, has always been the conflict between compassion versus output, alleviating poverty versus destroying work incentives, raising consumption versus distorting effort, government intervention versus market allocation; in short, redistributive goals versus efficiency goals.

Whatever the details of future proposals that extend benefits to the working poor, the program is likely to be controversial. Would a guaranteed annual income, delivered through refundable tax credits integrated with the personal income tax, be construed as purely a social program, since, Canadians would argue, it is intended solely to alleviate poverty and redistribute income? Or would such a scheme be labelled a trade-distorting subsidy to labour made on an unprecedented scale, since, the United States could argue, labour is by and large the single largest component of unit production costs? Since actual payments under a negative income tax are relatively more generous to lower-wage earners, and labour supply curves are not totally inelastic, comparative costs will also be affected, and hence trade distorting. The pith and substance test may be very difficult to apply. It is not easy to predict the outcome.

The same considerations will inevitably arise with respect to regional subsidies and development incentives. This is because the identical issue is involved, namely the extent to which Canada's social programs should be permitted to pursue redistributive goals (in this case, regional goals) in the presence of the CUSFTA requirement to safeguard free trade. Here again, difficulties arise because grants may go to producers who export a substantial portion of their output.

The importance of factor mobility in connection with a free trade area and the exchange rate regime has already been noted. There is another aspect of factor mobility which could have bearing on the financing of social programs in Canada. Historical experience reveals that people are relatively immobile, while capital generally moves freely across borders. Furthermore, corporations are most sensitive to after-tax returns, and ignore whatever social benefits governments give individuals. Hence high tax rates that finance large social expenditures will affect capital flows, even if the fiscal residua are everywhere the same. This implies two things. First, pressure to harmonize corporate tax-rate structures will be present, even if personal income tax systems differ extensively with respect to rate and progressivity. Second, given the relative sizes of the two countries, it is likely that Canada will have to adjust its corporate tax rate to be 'competitive' with the United States. This could severely limit the degree to which overall revenues in Canada can be raised from corporate taxes, leading to heavier taxes on

individuals, smaller total expenditures (including social spending) or both. Either way, Canada's social programs are affected.

Finally, with respect to social programs giving transfers to individuals, as well as those granting subsidies to regions or provinces, the Meech Lake Accord will amplify the impact of CUSFTA. If one believes, as many do, that Meech Lake has lessened the central government's power to establish national standards in social programs and to employ federal spending powers to shape national social policy, then individual provinces will stand alone when facing U.S. pressures to harmonize social benefits as a result of CUSFTA. No longer would provinces share a united Canadian front to oppose American demands. An already unequal contest may be made even more lopsided. Could, for instance, Nova Scotia on her own fight the Americans effectively over fish or seasonal unemployment benefits? However, the significance of the Meech Lake Accord for social policy is another story.

Concluding Observation

Despite the details that became available with the actual text of CUSFTA, much ambiguity remains. Will free trade with the United States result in harmonization of Canada's social programs with American policy? Only a preliminary answer is possible. Our judgment is that on technical economic considerations, any requirement to harmonize social programs is slight. Nonetheless, conclusions reached in the sixties concerning policy harmonization need to be modified. We suggested that the exchange rate must remain flexible at all times, but it cannot by itself be relied upon to combat high regional unemployment. Other conditioning factors -- tax reform and Meech Lake -- also impinge on the harmonization issue. In particular, pressures to adopt a value-added type of tax are now stronger. As well, the decentralization of government and thus of the power to mould a social welfare state may reinforce tendencies toward harmonization resulting from free trade. And finally, we suggested that most of Canada's social programs are likely immune from the charge of covert protectionism. Minor queries might be expected concerning some work-related programs, such as unemployment insurance and worker's compensation, and certain adjustments might be necessary to the delivery design. On the other hand, any major initiative that introduced earnings-related or income-tested payments

resembling a guaranteed income or negative tax scheme, might be construed as distorting trade.

The discussion so far has taken place entirely within the traditional economic approach. In other words, it formulates the question of harmonization in terms of the theory of tariffs, economic specialization, and the efficient allocation of resources. The assumptions implicit in this approach are that the objective is to maximize private consumption, and that all trade-distorting measures are arbitrary interferences with the free market. But there are many in Canada who view CUSFTA as essentially a non-economic matter. For them, free trade is but the codeword for continental economic integration, leading to loss of political sovereignty and cultural identity. This formulation is equally valid, and the questions it raises are equally difficult. When re-phrased in terms used by the traditional economic approach, these non-economic national objectives can be likened to a collectively consumed public good, so that what ought to be maximized is the consumption of private and public goods together. Government as well as the market are legitimate institutions with defined roles. Tariffs are not mere price distortions. The National Policy should have ended that fiction forever. As Johnson pointed out:

> if...government is regarded as an extra-market system for modifying the distribution of income and wealth, interest [should] focus on the tariff structure as measuring the political power of various claimants to the national income. . . .[29]

Canadians and Americans view CUSFTA from different starting assumptions and with different stakes. In particular, Canadians cherish a much stronger tradition of public intervention, hence, whatever else, they accept nation-building aims. For Canadians then, the categorization of CUSFTA as being simply a free trade deal struck to achieve economic benefits is biased ethically in favour of laissez-faire market principles. In this context, it is also subversive to claims that CUSFTA does not force conformity but merely bounds the permitted divergence between Canadian and American social programs. This could well translate into limits upon permitted differences in social values concerning income distribution, regional economic development, public services and the like.

The National Policy was less a policy about tariffs than a dream to forge a nation, east and west. So it is that CUSFTA is more than an agreement about the free flow of goods and services, north and south.

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NOTES

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2. **Globe and Mail**, September 30, 1985.
3. Drover, "Social Policy and Free Trade: Determinants of Harmonization." Unpublished manuscript.
4. Johnson, 1968, p. 2.
5. Lipsey and Smith, 1986, "An Overview of Harmonization Issues," in C. D. Howe Institute, **Policy Harmonization.**
6. Brean, 1986, pp. 44-45, "Fiscal Policy Harmonization and Negotiation of a Free-Trade Area," in C. D. Howe Institute, op.cit.
7. Hum, 1983, **Federalism and the Poor.**
8. Hum, 1984, "The Nature and Role of Social Services..." in **The Social Worker/le Travailleur Social.**
9. For example, Johnson, 1968, op.cit., Wonnacott, 1968, "Policy Harmonization in Free Trade Groupings..." and more recently, Lipsey and Smith, 1986, op.cit., and Brean, 1986, op.cit.
10. Johnson, 1968, op.cit.
11. Wonnacott, 1968, op.cit.
12. Johnson, 1968, p. 34, op.cit.
13. For example, Wilton and Prescott, 1987, **Macroeconomics: Theory and Practice in Canada.**
14. Lipsey and Smith, 1986, p. 16.

15. Brean, 1986, p. 45.

16. Magun, et. al., 1987, estimate the potential gains due to relaxing procurement policies to be slight for Canada, using assumptions different from the actual terms of the CUSFTA agreement. The conclusion is probably generally correct, nonetheless.

17. For further discussion of VAT, see Wonnacott, 1968, op.cit., Thirsk, 1987, "The Value-Added Tax in Canada: Saviour or Siren Song?" in **Canadian Public Policy**, and Cnossen, 1987, "VAT and RST: A Comparison," in **Canadian Tax Journal**.

18. Thirsk, 1987, op.cit.

19. Winer and Gauthier, 1982. **Internal Migration and Fiscal Structure.**

20. Wonnacott, 1968, pp. 62-63, op.cit.

21. Mundell, 1961, "A Theory of Optimum Currency Areas" in **American Economic Review** is the seminal statement. See also Hum, 1972, "Models of Optimum Currency Areas...", Ph.D dissertation.

22. Brean, 1986, pp. 59-60, op.cit.

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24. Hum, 1983, op.cit.

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SOCIAL POLICY HARMONIZATION: THE CANADIAN DEBATE, THE EUROPEAN AND TASMAN EXPERIENCES

Glenn Drover

The preoccupation with social policy harmonization is closely tied to Canadian concerns about political integration with the United States. To alleviate these concerns, proponents of the Canada - U.S. Free Trade Agreement (CUSFTA) suggest that the agreements of other developed countries offer little evidence of assimilation. Richard Lipsey and Murray Smith, for example, state that there is "no historical evidence to suggest that a high degree of trade liberalization between two countries leads to their political integration."[1] John Crispo echoes this sentiment by arguing that even the countries of the European Economic Community (EEC) -- whose founders intended to create a United States of Europe -- have not attained a high degree of integration.[2] The Macdonald Commission follows the same logic in asserting that the experiences of the countries associated with the European Free Trade Association (EFTA), the U.K. and Ireland, and the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) do not show cause for concern.[3] According to the Commission, free trade agreements "do not dispose the Irish to become more like the English" nor the New Zealanders to be more like the Australians.

While the current state of affairs seems to imply that free trade does not necessarily lead to political integration, the correlation between free trade and social policy harmonization is not so unambiguous. On the one hand, it is clear that free trade agreements, unlike common markets, have no implicit code of harmonization and appear to protect (by omission) the distinctive social programs of the trading partners. On the other hand, the experiences of countries associated with EFTA and ANZCERTA -- which provide the closest parallels to the bilateral agreement between Canada and

the U.S. -- indicate that there is a high degree of social policy harmonization. And even in the European Economic Community, where, in spite of specific treaty objectives to the contrary, social policy harmonization has been resisted in recent years, the similarities between existing programs seem to be greater than the differences. Thus, while the experiences of these countries may be highlighted to alleviate Canadian fears about political integration, the same cannot be said about social policy harmonization. To understand why a simple parallel cannot be drawn, it is necessary to review the current Canadian debate about institutional spillover, the free trade agreements of Europe and the Antipodes, and the institutional determinants of social policy. What the experience of other countries suggest is that harmonization is caused by institutional determinants, which are independent of, but closely associated with, free trade agreements.[4]

Institutional Spillover

In a general way, social policy harmonization relates to the concept of institutional integration or spillover.[5] Spillover refers to increasing integration resulting from degrees of association, varying from free trade to political union. While free trade partners lose some degree of political freedom, and the economic dependence of each economy increases, they are free to pursue other national interests which are not trade related. If, in the future, Canada wishes to pursue closer economic ties, it can move toward a customs union, a common market, or a common currency area. Each option, in turn, implies closer institutional and political ties. The customs union, because it involves a common tariff between the U.S. and Canada, would create a common commercial policy. A common market would, in addition, allow for the full mobility of labour. A common currency area means even closer political ties, as it implies a common central bank plus a closer alliance of debt and fiscal management.[6]

To explain spillover or institutional integration, neofunctionalists have posited a process of 'automatic integration,' beginning with free trade and leading to political union, or of 'cultivated spillover,' which implies that "a major political decision would be required to move toward advanced stages of integration."[7] While the likelihood of political integration, according to the neofunctionalists, will occur only after two nation states are committed to a common market, one cannot ignore the possibility for

spillover at the level of free trade, particularly when, as in the case of Canada and the U.S., the relative economic strength of the two partners is uneven.

In contrast to the neofunctionalist perspective, dirigist theorists postulate that spillover results from imbalances created by minimal forms of integration, which lead to pressures for corrective action resulting in closer cooperation.[8] The imbalances are likely to be greater when there is economic asymmetry between the partners or within the partners' respective societies (regional imbalances, for example).[9] This can happen because the initial freeing-up of goods and services caused by free trade highlights initial imbalances, which in turn lead to demands for higher levels of integration. If the appropriate corrective measures do not occur, there is a tendency for the imbalances to be entrenched through national action, thereby "strengthening the competitive position of the stronger partner."[10] Spillover is not automatic, but the overall probability of integration in a free trade zone is likely to be highly associated with the increased development of transnational institutions (e.g., joint initiatives in a variety of fields), public dissatisfaction with the limits to free trade benefits (as occurred in the early free trade agreement between Australia and New Zealand) or the unequal distribution of benefits in the free trade area that cannot be corrected by unilateral action. In each of these cases, the propensity to policy harmonization, including social policy, could be significant.

The spillover thesis has both detractors and advocates within Canada. Paul and Ronald Wonnacott were among the early detractors of the spillover thesis. In a 1967 landmark study, they concluded that Canada would receive net gains in a free trade agreement with the U.S. primarily because of lower wage and resource costs, but also because of an increase in efficiency due to additional competition. With respect to social policy, the Wonnacotts were silent except insofar as they cautioned against a customs union or a common currency area because of the implicit political commitment to which such agreements would lead. Even so, they essentially were sceptical about the likelihood of spillover.[11] Seven years later, in a study for the Economic Council of Canada, Ronald Wonnacott again documented the economic advantages of free trade. Still, there was no specific concern about the potential for spillover.[12] However, in a companion report issued by the Economic Council, the spectre of political union

and 'cultural' or 'social' integration was directly addressed.[13] While the Council was not concerned that a Canada-U.S. free trade agreement would lead to political absorption, it cautioned against prolongation of existing trading practices, which could, in the long run, be more detrimental to Canadian independence than an economic relationship based on an agreement.

Essentially, the Council followed Peyton Lyon, who adamantly opposed the spillover thesis.[14] Lyon affirmed that there was no evidence to support the prediction that a free trade agreement would drive Canada and the United States to a higher level of integration. He suggested instead that an agreement would lead to a new 'dynamic equilibrium' and possibly a new national awakening. By contrast, his colleague Charles Pentland wrote in the same report that two other outcomes were also possible -- either enhanced resistance (due to renewed nationalist sentiment) or further integration (due to the lulling of nationalist fears). The 'dynamic equilibrium' of Lyon, rather than Pentland's more pessimistic possibility, was favoured ten years later when the Macdonald Commission took its stand in support of free trade.

Three other recent studies that have also implicitly rejected spillover are by Charles Doran, Richard Lipsey and Murray Smith.[15] Doran's study is based upon quantitative analysis. He concludes that independence will not be adversely affected by close trade ties, but draws no firm conclusion about social programs given the limitations of his data. Lipsey and Smith disagree with spillover because they find no convincing evidence of it in Europe, because they see no interest on the part of the U.S., and because Canadians are attitudinally different from Americans.[16] In a subsequent report specifically focused on policy harmonization, they acknowledge that spillover pressures are present between the U.S. and Canada in the cultural and social areas, but that general fears have to be separated from specific consequences of the agreement. In general, they conclude that Canada's social programs are essentially protected by a fluctuating exchange rate and a broadbased tax system.[17]

The advocates of spillover generally take the opposite tack. Throughout the past decade, Mitchell Sharp has opposed a bilateral free trade arrangement because of his concern about sovereignty. "My misgivings about a free trade agreement between Canada and the United States," he says, "relate not to the economic

consequences but to the effect of such a bilateral, preferential agreement upon Canadian independence."[18] The effect that he fears is the gradual absorption of Canada into the United States.

Another advocate of spillover is Abraham Rotstein. While not opposed to free trade through GATT, he is particularly wary of a bilateral arrangement with the Americans for two essential reasons. The first is the American concept of a 'level playing field.' The concept refers to ground rules for trade that are consistent with U.S. practice. Under the level-playing-field approach, he believes the Americans would want guarantees that Canada will not directly or indirectly subsidize its industries in competition with the U.S. In terms of social policy, this means, according to Rotstein, that without control over American countervail, any Canadian subsidy -- including subsidies presumably inaugurated for social purposes -- might be deemed unfair. "The only real option" he says, may be for Canada "to conform to existing American practices."[19] Exchange rates and tax rates, if widely divergent from the United States, might also be subject to pressures or manoeuvres that restrict an open exchange rate policy and foster the harmonization of tax rates.

B. W. Wilkinson also acknowledges that free trade with the U.S. could increase pressures for integration. In fact, he states the integration of Canada into the United States is already so great "that one has to ask what it is that we are attempting to preserve."[20] Like the Economic Council of Canada, he seems to imply that planned liberalization has at least the merit of allowing Canada to negotiate the terms of sovereignty, assuming that the federal government is clear about what it wants to safeguard, and assuming further that U.S. goodwill is tolerant of Canadian aspirations. If either assumption is weak, he implies that annexation between the two countries is a very real possibility.

To back up his assessment, Wilkinson points to two previous free trade agreements -- the Zollverein and the Hawaiian -- which did in fact lead to integration. The 1870 Zollverein (which stipulated a customs union rather than free trade) was an agreement involving Prussia and its surrounding sovereign states. While the agreement need not have led necessarily to the gradual emergence of Germany, it did so for two apparent reasons. The first is that the disproportionate economic strength of Prussia made it difficult for the other German states to

opt out of the agreement once free trade had become a reality. The second is that a common language as well as a common cultural heritage made it difficult to resist integration, even though the "path from economic to political union was not a smooth one."[21]

The first reciprocity treaty of 1855 between Hawaii and the United States covered agricultural products. It was essentially a limited free trade agreement. In 1875, it was expanded to include other goods after Hawaii agreed to limit any privileged access to harbours or land by any other power than the U.S. In the mid-1890's, an annexation club was initiated in Hawaii with the support of the U.S. administration. The push for annexation within the U.S. was mainly motivated by the commercial advantage of the island, and eventually in 1898 Hawaii became a part of the United States. On the road to annexation, according to Wilkinson, the limited diversification of the Hawaiian economy was widely debated by the Hawaiians themselves but never resolved. The U.S., not Hawaii, decided upon annexation after the Americans realized it was in their long-term interest.

Still another advocate of spillover is James Laxer. In his book, **Leap of Faith**, Laxer asserts that economic ties with the U.S. are not really about free trade, but about Canadian sovereignty.[22] He also states that closer affiliation with the U.S. market is affiliation with an industrial economy in decline, an industrial economy failing to adapt. Why then, according to Laxer, attach our future to a falling star? Why subordinate the Canadian way of life to the American? In response to the latter question, Laxer points to the pivotal role of Canada's social policies and social programs -- programs which help to make our cities less violent than those of the U.S., our income disparties less extreme, our provision of services for the sick, the old, the unemployed and the disadvantaged, more acceptable. Laxer is less concerned about the integrity of Canada's social programs if free trade is only about the removal of tariff barriers.

Like Rotstein, he also is concerned about the American level playing field. Canada has survived, in part, because of large-scale government intervention. In areas varying from railways to culture to health care and unemployment insurance, programs have evolved in ways which are the antithesis of the American "belief in the ability of the market place to set priorities for society."[23] What is important to the U.S. is the American identity, an identity built messianically on a

marketplace ideology. It is a society, according to Laxer, with limited tolerance for forms of social intervention and collective consumption. And "the idea that a smaller country needs special measures to protect its identity does not resonate south of the border. Such an idea smacks of state intervention. It is an affront to the free working of the market system and therefore to the American way of life."[24] Therefore, even if social programs are explicitly excluded from an open trade agreement, they will be subject to the scrutiny of an eagle eye.

The common message of other critics, including A.N.T. Varzeliotis, Jim Turk and Sam Gindon, is that a free trade agreement will be an effective restraint on Canadian social programs and possibly lead to harmonization.[25] Even Ian Drummond, who is not necessarily opposed to free trade, believes that pressure toward harmonization will continue in the future. For that reason alone, he suggests that it would be better to opt for a common market in order "to negotiate a 'code of harmonization'."[26]

The advocates of spillover, like its detractors, rely upon an analysis which, while coherent and persuasive, is largely deductive and speculative in nature. Both sides speak in general terms about integration without specifically addressing social policy. Furthermore, neither side has identified the institutional determinants of social policy harmonization, and neither side has closely examined how existing agreements in other parts of the world have accommodated national social policy and free trade interests. Three recent agreements pertinent to this question are the European Free Trade Association (EFTA), the Australian New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) and the European Economic Community (EEC).

Free Trade Agreements In Europe And The Antipodes

EFTA, established in 1960 in partial response to the EEC, currently involves Austria, Iceland, Norway, Sweden, Switzerland and Finland. It formerly included Great Britain, Denmark, and Portugal before their entry into the EEC. Unlike the EEC, however, EFTA joined together countries who were not explicitly interested in political integration, or who were excluded from association with the EEC because of other international agreements.[27] In the EFTA (Stockholm) convention, the rules which govern policy coordination that possibly affect the internal social policies of the member

countries are those relating to government aids and internal taxation, if the latter in some sense restricts the benefits expected from the elimination of tariff and non-tariff barriers.[28] Such practices, while not expressly prohibited, are considered to be incompatible with the convention. Compliance is voluntary. There is no binding mechanism for dispute settlement. One consequence is that any export perceived to be unduly levied (including social welfare charges) would be forbidden unconditionally if the assumed benefits of free trade are frustrated. Similarly, taxes or tax expenditures aimed at providing "an artificial stimulus to the export capacities of home industries" are prohibited.

Unlike the bilateral agreement between Canada and the U.S., which combines some aspects of a common market,[29] EFTA is very restrictive in its terms of trade.[30] The EFTA convention essentially creates free trade for industrial goods. Thus, it excludes agriculture and services, while permitting only a limited movement of labour and capital. The controls on agriculture were initiated for pragmatic reasons. But the limits over capital and labour, and to a lesser extent, services, were intentional in order to preserve the cultural identity of the member countries.[31]

There is some evidence that trade liberatization has led to institutional spillover through administrative and consultative structures established under the convention. Like the bilateral agreement between Canada and the United States (CUSFTA), the convention simply states that the "institutions of the Association shall be a Council and such other organs as the Council may set up."[32] In practice, this has meant that the Council has established whatever committees it has deemed important. Two committees pertinent to social policy areas are the Consultative Committee (with its Economic and Social Subcommittee) and the Economic Committee, both of which address broader questions than those arising from technical applications of the agreement. The Consultative Committee also follows the corporatist traditions of Europe in having a strong representation from labour as well as business. In recent years, the committees have shown increasing interest in unemployment, regional development, social problems resulting from economic changes, and state aid.[33] The impact that the committees have had on social policies is difficult to determine, but the Consultative Committee -- and other committees as well -- does seem to reflect the broader economic structures, including

the corporatist structures characteristic of countries like Sweden, Norway, and Austria. Their inclusion is significant because the corporatist structures have an influence on social policy harmonization.

ANZCERTA, like EFTA, had its origins in the 1960s when its predecessor -- the New Zealand-Australia Free Trade Area (NAFTA) -- was established.[34] However, NAFTA was restricted to only a limited range of commodities, which was not expanded until the formation of ANZCERTA in 1983. Under the agreements, two countries with a "common language, shared political institutions, free movement of peoples, and closely linked financial, commercial and service sectors"[35] have also set in motion additional measures for bilateral economic integration and policy coordination. For some observers of free trade, the shift from NAFTA to ANZCERTA is clear evidence of a spillover effect.[36] Under NAFTA, trading arrangements were initially institutionalized for consultation between politicans, government officials and businessmen on both sides of the Tasman Sea. Under ANZCERTA, they were expanded to include a formal agreement on agricultural and industrial goods.[37] At the same time, there was no agreement on services and no formally established bilateral dispute mechanism.[38] Like EFTA, the continuance of support and stablization measures for agriculture was also considered important to the welfare of the two countries.[39]

The newest Tasman agreement, which has no explicit statement about the need for harmonization of social policies, was nevertheless concluded by two countries with long-held views about social programs. Both countries maintain broadly based coverage and centrally funded health care. Tax reforms, based upon similar principles of equity and the closing of special privileges, recently have been introduced. Both countries have been pioneers in worker's compensation and unemployment relief.[40] Both have similar levels of social expenditures. Like the corporatist states within EFTA, therefore, the tendency toward harmonization in social areas seems to have proceeded in tandem with a free trade agreement. The same cannot be said of Canada and the United States.

In contrast to Australia and New Zealand, the countries of the EEC are very diverse linguistically and culturally. During their histories, they have fought with each other. They have differing political ideologies. They have disparate structures of

government. They vary in size. They represent widely differentiated levels of economic development. They enjoy considerable national autonomy. In spite of these differences, however, six nations of Europe, under the Treaty of Rome in 1958, came together to form a common market for the free movement of goods, services and labour in order to enhance the overall standard of living of the participating partners. Initially, the common market included Germany, France, Italy, the Netherlands, Belgium and Luxembourg. It now also incorporates Denmark, Greece, Ireland, Portugal, Spain and the United Kingdom. Unlike EFTA, ANZCERTA and CUSFTA, the Treaty of Rome, in addition to supporting the formation of a customs union, also fosters a common labour market. Hence, the treaty actually specifies the terms and conditions for the harmonization of social and fiscal, as well as economic policies.[41]

Under the terms of the treaty, the free movement of persons, services and capital is progressively guaranteed, as is the movement of goods. The effect of the agreement in agriculture, however, is the creation of a managed market, which takes into account its special social structure and the need to make appropriate adjustments gradually.[42] To further institutional integration within the community, the treaty also establishes a representative assembly, a Council of Ministers, an Administrative Commission, and a Court of Justice. In addition, it sets up an Economic and Social Committee, representative (like the EFTA Consultative Committee) of major employer and employee associations, to advise the Council on matters pertinent to the implementation of the treaty.

The key terms for social harmonization are Articles 117 and 118. They read (in part) as follows:

> Member States agree upon the need to promote improved working conditions and an improved standard of living for workers, so as to make possible their harmonization while the improvement is being maintained. (Article 117)[43]
>
> Without prejudice to the other provisions of this Treaty and in conformity with its general objectives, the Commission shall have the task of promoting close cooperation between the Member States in the social field. (Article 118)[44]

It is not surprising that the treaty explicitly refers

to social policy harmonization, since one objective of a common market, unlike a free trade zone, is to facilitate the free and efficient mobility of labour. What is surprising is that the provisions rarely have been used to foster such harmonization. Doreen Collins, after reviewing the first fourteen years of the EEC, had to conclude that social policy remained essentially a national rather than a community responsibility.[45] Her assessment has been confirmed more recently by John Holloway.[46] According to Collins, there are many reasons why, in spite of specific treaty provisions, social policy has remained a national responsibility under the EEC. The first is that viable social programs require "an advanced system of government which stems from a well-knit, self-conscious national identity."[47] The second is that social policies reflect different political expectations, which are commensurate with national needs. The third is that the institutions of the EEC are remote from the day-to-day life of the people. The fourth is that the community has never had the power to harmonize policies in the face of the intransigence of national governments. The fifth is the ambiguity of Articles 117 and 118.

Holloway elaborates upon the latter point. He notes that throughout the brief history of the EEC, two approaches to the interpretation of Articles 117 and 118 can be distinguished. A narrow interpretation -- favoured by employers and the Council of Ministers -- is that the articles do little "to restrict the autonomy of the member states in the social field and do not establish a basis for a general Community social policy."[48] A more comprehensive interpretation -- promoted by the unions and members of the EEC Commission -- is that the articles establish goals for member states, which should be guidelines for improving living standards and workers' wages. Support of the comprehensive interpretation accept the French version of the text, which suggests there should be "égalisation dans le progrès."[49] Opponents argue that 'égalisation' does not mean uniformity or unification, but simply an improvement in living and working conditions as a result of the progressive functioning of the market itself.

The impasse resulting from the ambiguity of different interpretations of the articles of the treaty has meant that up to the present,the EEC has played a subordinate role to national governments in the development of social policies. At the same time, this does not mean that there has been no attention given to harmonization. At a minimum, the treaty requires the commission to

provide comparative studies and deliver opinions, in consultation with the Economic and Social Committee, on problems of social policy that arise at national levels or interfere with the functioning of the market. It also explicitly recognizes that economic and social progress go together. Further, it has fostered increasing cooperation between employers and workers through seminars and conferences.[50] In addition, it has coordinated programs so that migratory workers of the EEC are treated as 'nationals' for purposes of social security.[51] And finally, it has created The European Social Fund to assist in the retraining of unemployed workers.[52]

Nevertheless, with the exception of the fund, the initiatives have been voluntary in nature, and harmonization, to the extent it has occurred, seems to have resulted from institutional commonalities within member states (e.g., the active influence of the labour movement in national policies, and national corporatist structures for settling wage rates, including social wages) rather than the institutional structures of the EEC. The community structures, such as the commission and the committees which oversee social policies, have had an indirect influence on the integration of social policies through study reports and consultation. Their role has been secondary, not primary. As in the case of EFTA and ANZCERTA, therefore, institutional forces outside the agreement seem to account more for harmonization than do the formal treaties.

Institutional Determinants of Social Policy

Lipsey and Smith state that "the most important requirement for talking sensibly about the whole harmonization issue is to distinguish between pressures that now operate and those that would actually result" from a free trade agreement.[53] They then go on to distinguish between harmonization that would result from post-agreement pressures operating in the Canadian economy, and specific terms of the Agreement which may limit Canadian independence. With respect to the former, they conclude that pressures for harmonization of unemployment insurance, medical care, pensions and other broad-based programs such as family allowances, maternity benefits, education and social services will be unaffected because they influence all Canadian industries equally. To the extent that adaptations are required, they will occur through adjustments of the exchange rate. With respect to the terms of the Agreement, they see no compelling economic reasons why

social programs would be affected, but they acknowledge that pressures toward harmonization could increase due to political misunderstandings and complex regulatory policies emanating from trade in services.[54]

From a review of the Canadian debate on bilateral free trade and the free trade agreements in Europe and the Antipodes, it appears that there is no simple answer to the question of whether post-agreement pressures will enhance social policy harmonization. The inconclusive nature of the debate on spillover and experiences elsewhere suggest that free trade does not automatically lead to harmonization even in common markets. On the other hand, the evidence provides no assurance that social policies will be unaffected by free trade because they are not explicitly addressed in a formal agreement. The reason why neither polar position seems accurate is that social policy harmonization is likely to result from pressures which, while not necessarily caused by free trade, are related. A direct relation between free trade and social policy is unlikely unless other institutional pressures combine to encourage integration.

Before turning to a closer examination of other institutional determinants in Europe and the Antipodes, it is important to indicate in broad terms the extent of harmonization of social programs in the countries of the EFTA, ANZCERTA and the EEC, compared to CUSFTA. While, as already noted, there has been resistance to harmonization through the EEC by business interests and governments, the resistance does not detract from the fact that a considerable degree of similarity in program principles already exists, even though national governments largely remain responsible for social policies. The similarity is demonstrated in an early study by J. Van Langendock of health insurance among the original six countries of the EEC.[55] He describes how, by the early seventies, there were broadly accepted principles of health care and comprehensive medical care benefits in all the countries, even though there were (and remain) many variations in administrative and financial structures, such as whether payroll deductions or general tax revenues are used to fund services. This similarity is also demonstrated in a later study by Vic George and Roger Lawson, who, while criticizing the political will of EEC governments to resolve problems of poverty, recognize many commonalities in social security schemes.[56]

A general picture of the social programs throughout the countries of EFTA, ANZCERTA, the EEC and CUSFTA can be appreciated by reference to Table 1. The table indicates that every country, including the U.S., has some sort of comprehensive coverage for old age and invalidity insurance, work injury compensation, and unemployment. In contrast with all other countries, the U.S. does not have national sickness and maternity benefits, comprehensive medical care or hospital coverage. Along with Iceland, the U.S. also shares the distinction of not having a family allowance scheme. Hence, it is evident in very broad terms that with the exception of the U.S., the free trading nations of Europe, Australia, New Zealand and Canada have achieved a minimum level of social policy harmonization.

Harmonization can also be circumscribed by the tendency of countries to follow organizing principles of universalism or selectivism, social insurance or social assistance. In general, the countries of EFTA and the EEC, like Canada and unlike the United States, favour universalism and social insurance over selectivism and assistance. Australia and New Zealand have a mixed approach. Within EFTA, for example, all countries except Iceland have social insurance schemes for old age, invalidity and death. Iceland has a universal tax-funded pension in lieu of insurance, and some countries (such as Finland, Norway, and Sweden) have, like Canada, a dual universal and social insurance system. With respect to sickness and maternity benefits, all countries except Iceland and Switzerland have instituted a social insurance scheme, usually through employer/employee contributions supplemented, as necessary, by government revenues. In Iceland, a universal system is funded by national and local governments; in Switzerland, a mixed compulsory and voluntary scheme is funded through government revenues and membership fees in approved funds.[57]

Work injury compensation in all EFTA countries is based on social insurance, but varies by the type of carrier. Finland authorizes employers to insure liability with private insurance companies; Switzerland has a semi-public carrier. Unemployment is more variable. In Austria, Norway and Switzerland, compulsory insurance schemes are administered by governmental bodies. In Iceland, Finland and Sweden, dual subsidized voluntary insurance, administered by unions or employee associations, is supplemented by government-sponsored unemployment assistance.

TABLE 1

Social Security Programs By Type
1985

COUNTRY	TYPE OF PROGRAM					
	Old Age & Invalidity	Sickness & Maternity	Medical Care	Work Injury	Unemployment	Family Allowance
EFTA						
Austria	x	x	x	x	x	x
Iceland	x	x	x	x	x	
Finland	x	x	x	x	x	x
Norway	x	x	x	x	x	x
Sweden	x	x	x	x	x	x
Switzerland	x	x	x	x	x	x
ANZCERTA						
Australia	x	x	x	x	x	x
New Zealand	x	x	x	x	x	x
EEC						
Belgium	x	x	x	x	x	x
Denmark	x	x	x	x	x	x
France	x	x	x	x	x	x
Germany	x	x	x	x	x	x
Greece	x	x	x	x	x	x
Ireland	x	x	x	x	x	x
Luxembourg	x	x	x	x	x	x
Netherlands	x	x	x	x	x	x
Portugal	x	x	x	x	x	x
Spain	x	x	x	x	x	x
United Kingdom	x	x	x	x	x	x
CUSFTA						
Canada	x	x	x	x	x	x
United States	x			x	x	

Source: U.S. Health and Human Services, Social Security Administration, Social Security Programs Throughout The World 1985, Research Report #60, July 1986.

TABLE 2

Total Tax Revenue & Social Security Contributions As A Percentage of GDP 1985

COUNTRY	Tax Revenue	Social Security
EFTA		
Austria	42.5	13.5
Finland	37.3	3.4
Norway	47.8	9.9
Sweden	50.5	12.5
Switzerland	32.1	10.3
ANZCERTA		
Australia	30.3	--
New Zealand	34.3	--
EEC		
Belgium	46.9	15.5
Denmark	49.2	1.9
France	45.6	19.9
Germany	37.8	13.8
Greece	35.1	12.2
Ireland	39.1	5.8
Italy	34.7	12.1
Luxembourg	42.8	10.9
Netherlands	45.0	19.7
Portugal	31.1	8.1
Spain	28.8	12.0
United Kingdom	38.1	6.7
CUSFTA		
Canada	33.1	4.4
United States	29.2	8.6

Source: OECD, Revenue Statistics, 1965-1986, Paris 1987, Tables 3 and 14.

Similarly, family allowances are universally available except in Iceland, but vary in terms of financing mechanisms. Austria and Switzerland rely in part on payroll deductions; the others depend entirely on government financing to cover the cost.

Turning to ANZCERTA, one notes that the social security programs, while providing basic coverage like the EFTA countries, are nevertheless closer to each

other organizationally than are their European counterparts. Old age, invalidity and death benefits, for example, rely upon dual universal and social assistance rather than social insurance. In sickness and maternity, the approach is also dual universal and social assistance, as is the case with family allowances. The assistance method also distinguishes unemployment, in contrast to the insurance schemes of Europe. One area where Australia and New Zealand differ is with respect to work injury compensation. While the latter country has a comprehensive universal and social insurance system to cover all accidental injuries regardless of cause, Australia provides compulsory insurance for employed persons only.[58]

The twelve countries of the EEC also display a remarkable degree of similarity with respect to basic organizing principles.[59] In terms of old age, invalidity and death benefits, all countries have schemes based on social insurance. In three countries, the social insurance programs are supplemented: in the United Kingdom and Ireland, by assistance systems, and in Denmark, by a universal pension. Sickness and maternity benefits are provided in all cases through national social insurance, and medicare is provided in the same fashion except in three countries which have nationally administered schemes (the United Kingdom, Ireland and Denmark). Work injury compensation, like EFTA countries, varies to the extent that some countries mandate or permit private rather than public carriers (Portugal, Germany, Denmark and Belgium). The Netherlands, like Sweden, provide similar compensatory benefits to all residents, regardless of the cause (or source) of the accident. In terms of unemployment, four countries supplement insurance schemes by assistance (France, Ireland, the Netherlands and Portugal). Family allowances seem, however, to vary considerably -- five countries have employment-related systems, and seven have universal programs.

Another way in which social program comparisons can be made among member countries of trading associations is through an examination of government finance. Table 2 provides information on total tax revenue and social security contributions as a percentage of GDP. From the table, we can see some common patterns. Among the EFTA countries (with the exception of Switzerland), tax revenues are high compared to ANZCERTA and CUSFTA, but similar in range to the richer countries of the EEC. Social security contributions are more variable, depending upon the proportion of social security

TABLE 3
Social Expenditures
1981

COUNTRY	% GDP	SOCIAL EXPENDITURE % Total Expenditure			
		Education	Health	Pension	Unemployment
EFTA					
Austria	25.9	13.7	17.1	49.8	1.8
Finland	26.0	24.1	19.9	33.9	2.3
Iceland	--	--	--	--	--
Norway	27.1	22.5	23.6	29.2	1.1
Sweden	33.5	19.8	26.6	35.3	1.5
Switzerland	13.9	--	--	--	--
ANZCERTA					
Australia	17.6	30.9	25.0	29.8	4.3
New Zealand	18.6	23.0	24.5	37.2	2.6
EEC					
Belgium	35.0	20.5	13.3	23.9	6.9
Denmark	31.8	--	--	--	--
France	29.1	19.3	22.0	40.3	6.4
Germany	29.2	16.5	20.6	39.7	4.4
Greece	13.1	17.9	26.1	42.5	2.2
Ireland	25.1	25.0	29.6	18.3	8.8
Italy	26.2	22.0	20.6	45.4	2.4
Luxembourg	--	--	--	--	--
Netherlands	33.9	19.7	18.6	36.0	2.8
Portugal	--	--	--	--	--
Spain	--	--	--	--	--
United Kingdom	23.1	24.5	22.8	31.2	5.9
CUSFTA					
Canada	22.1	28.8	26.0	31.4	10.7
United States	20.2	26.4	20.2	35.6	2.4

Source: OECD, Social Expenditures 1960-1990, Paris 1985, Tables 3 and 4.

programs funded out of general revenue or payroll deductions.

Still another way of making a comparison is to look at all social expenditures including health, education and welfare services, as well as social security (Table 3). Within EFTA, Austria, Finland, Norway and Sweden have relatively high social expenditures (in excess of 25 per cent) but Switzerland is low. The largest expenditures in all countries are on pensions, regardless of the overall level. In ANCERTA, the proportion of expenditures going to health, education and pensions varies between countries, but total social expenditures as a percentage of the GDP are comparable. The same is also true of Canada and the U.S. Within the EEC, like EFTA, there is more variation in total social expenditures when a poorer country, like Greece, is taken into account. However, among the richer countries of northern Europe, social expenditures (with the exception of the United Kingdom) generally exceed 25 per cent of GDP.

The essential question is how are we to interpret these data with respect to the free trade agreements? We have noted that the European and Tasman agreements generally have not explicitly stipulated the need to harmonize social policies, while the EEC has given social policy harmonization a lukewarm reception in spite of specific harmonization objectives. We also have seen that social security programs among countries within trading blocks frequently approximate each other in principle and, in several instances, expenditure patterns as well. The answer to the discrepancy lies, in part, in the institutions set up in countries to develop and administer the welfare state. In Europe, corporatist structures -- representing business, labour and government -- have played a key role. In Australia and New Zealand, social democratic institutions and labour organizations have been pivotal.

Corporatist structures evolved in post war Europe to provide a way of creating harmony between labour and management. They generated consensus around the welfare state so that labour organizations could have an important voice, at least in matters of social security and social services.[60] Recently Harold Wilensky has sought to explain the stability of the European social welfare state using corporatism as a major variable. He concludes that "corporatist democracies can tax, spend, and yet stay cool."[61] Robert Kuttner claims that they also serve to encourage interdependence among

conflicting social groups, in contrast with the pluralism of the United States, which emphasizes individualism and divergence.[62] Lester Thurow similarly alludes to the need to explore institutional structures like corporatism in the U.S. in order to introduce flexibility and encourage competition.[63]

Writing more explicitly about the role of corporatism within the welfare states of North America and Europe, Ramesh Mishra makes somewhat the same point. He compares the case of Austria (where a joint committee of labour and management meets monthly, with the Chancellor in attendance, to make decisions that are recommended to government) to the antagonism between labour and management in Britain. In Austria, a long-term voluntary prices and wages policy had been worked out in the early 1980s, which allowed the economy to function smoothly during subsequent periods of international instability. By contrast, a wages policy imposed by the British government at the same time simply delayed the unions' push for higher pay and eventual high inflation rates. The corporatist structures of Austria -- like those of France, Germany, Sweden, the Netherlands and Norway -- also contribute to an integrated social policy.[64] They serve to establish priorities for the redistribution of societal resources. They accommodate regional interests. They foster opportunities for the disadvantaged. They recommend appropriate levels of social expenditures.[65]

The welfare states of Australia and New Zealand have not the same kind of institutional structures as those in Europe. What they do share, however, is a parliamentary system, a similar historical heritage, an active labour movement, and a viable tradition of social democracy. In addition, because of their relative geographic isolation, Australia and New Zealand have often turned to each other in order to develop their social programs. In this fashion, the first pension schemes of Australia were heavily influenced by New Zealand, and each country has helped to pioneer programs like minimum wages and workers compensation through the welfare state.[66]

By contrast with EFTA, ANZCERTA and the EEC, Canada and the United States have few common institutions that have harmonized their social programs. In Canada, a tradition of government intervention in the economy has prevailed since Confederation. There also has been a social democratic influence in political life, as well as a British heritage of parliamentary government. In

the United States, none of these institutional patterns have been dominant. On the other hand, what the two countries do share is a high degree of economic integration through multi-national (mostly American) corporations. The penetration of American corporations into the Canadian economy has been documented by many scholars over the past twenty years.[67] However, it bears repeating that when one considers Canada's "free trade arrangement with the U.S., along with the three-quarters of Canada's import and export trade that is accounted for by Americans, and the nearly one-half ownership share of our productive instruments that they now enjoy, it is difficult to avoid the conclusion that the Canadian economy looks less like a distinct national economy and more like a geographically large zone within the U.S. economy.[68] "More than any other socio-economic institution, it is the extensive penetration of American corporations in Canada which makes the Canadian-American trading relationship unique.

Implications for Canada

The review of the free trade experience in Europe and the Antipodes has two important implications for the free trade debate in Canada. The first is that CUSFTA is more comprehensive than either EFTA or ANZCERTA. The second is that the socio-economic institutions of the welfare state play an important role in social policy harmonization.

CUSFTA, ANZCERTA and EFTA agreements all have one thing in common with respect to social policy: none of them, like the EEC treaty, invokes a code of harmonization. Beyond that commonality, however, they vary. EFTA is the more circumscribed of the free trade agreements in creating essentially a free trade area in industrial goods, while excluding agriculture and services, and providing only for the limited movement of labour and capital. ANZCERTA goes one step further in opening up the agricultural area, but is silent in all other areas. The EEC treaty, by contrast, calls for essential free trade in all areas while allowing for controls in agriculture because of its sensitive role in each country. Hence, by comparison with CUSFTA, the free trade countries of EFTA and ANZCERTA have been more cautious in integrating their economies. The contrast is noted in a recent study by Victoria Price on the free trade areas of Europe. She writes:

> Canada and the United States, whatever the problems that divide them, start from a different

> perspective. In many ways, they are already integrated, so integrated in fact that the preservation of a distinct cultural identity appears to be a problem for Canada, the smaller of the two. The key question for Europe was, and still is, how to overcome diversity in order to reap the benefits of economic integration. The key question for Canada and the United States, on the other hand, is how to reap the benefits of economic integration while preserving diversity.[69]

To the extent that EFTA, ANZCERTA and the EEC are different from CUSFTA, they do not provide a clear model upon which to make any predictions about the effect of a free trade agreement on Canadian social policy. A more useful approach to understanding the potential impact is to consider the institutional determinants of harmonization. In Europe, the corporatist institutions of the welfare state have played an important role in harmonizing social policy. In Australia and New Zealand, a common political heritage seems to have been pivotal. In general, the countries of Europe and the Antipodes have social programs which, while by no means identical, have been developed along similar principles of universalism and social insurance. And while the harmonization of social policies cannot be attributed directly to the free trade agreements, the latter, at least in the case of Europe, allow for consultative bodies that reflect to some degree the corporatist structures which have been determinant.

In Canada and the United States, there are no equivalents to the well-entrenched corporatist structures of Europe or the common social democratic experiences of the Antipodes. Nor are there shared political institutions. Instead, there is a common heritage of American corporations. In the recent past, American corporations have not functioned to harmonize the social programs of the two countries -- due largely to a strong sense of Canadian identity and a growing economy -- but whether they chose to do so in the future remains to be seen. However, to the degree that they attempt to harmonize the social policies of the two countries, and to the extent that institutional determinants are pivotal to harmonization, so they will attempt to limit the autonomy of the Canadian welfare state. This is not to imply that the Canadian welfare state will necessarily lose its capacity to introduce its own social programs. At a minimum, it can always rely upon age-old concerns of American domination to

reassert Canadian content. Nevertheless, what it does mean is that the State's ability to manoeuvre could be considerably restricted if the corporations exercise their institutional muscle. Furthermore, to the extent that the terms of the bilateral agreement reinforce the institutional muscle, they could, like the treaties of Europe, contribute indirectly to social policy harmonization.

NOTES

1. Lipsey and Smith, 1986a, p. 91.
2. Crispo, 1985, p. 308f.
3. Royal Commission, 1985, p. 352.
4. Social policy harmonization refers to the tendency of the social programs of two or more countries to converge along the same organizational principles. It does not necessarily imply that the programs will become identical.
5. Haas, 1968; Soldatos, 1985.
6. Wonnacott and Wonnacott, 1967, 1968.
7. Saldatos, 1985, p. 166; also Pentland, 1973, Chapter 4.
8. Taylor, 1980.
9. Soldatos, 1985, p. 174.
10. Ibid., p. 177.
11. Wonnacott and Wonnacott, 1968, p. 8.
12. Wonnacott, 1975.
13. Economic Council, 1975.
14. Lyon, 1975.
15. Doran, 1983; Lipsey and Smith, 1986a,b.
16. Lipsey and Smith, 1986a, pp. 91-95.
17. Ibid., p. x.
18. Sharp, 1987, p. 3.
19. Rotstein, 1985, p. 324.
20. Wilkinson, 1985, p. 292.
21 Ibid., p. 299.
22. Laxer, 1986.
23. Ibid., p. 96.

24. Ibid., p. 101.
25. Varzeliotis, 1985; Turk, 1985; Gindon, 1986.
26. Drummond, 1986, p. 64.
27. EFTA Secretariat, 1966, pp. 11-14; Price, 1987, p. 2f.
28. Shibata, 1986, p. 76.
29. Wilkinson, 1987, p. 223.
30. Price, 1987, pp. 7-12.
31. Price, 1987, p. 9.
32. EFTA Secretariat, 1976, pp. 94, 112.
33. EFTA Secretariat, 1980, pp. 30-32; 1987, pp. 19,24.
34. Gold and Thakur, 1982; Thomas, 1976.
35. Thakur and Gold, 1983, p. 83.
36. Soldatos, 1985.
37. Kirby, 1984; Thakur and Gold, 1983.
38. New Zealand, 1983.
39. Gold and Thakur, 1982, p. 407.
40. Albinski, 1986, p. 150f.
41. European Economic Community, 1958.
42. Price, 1986, p. 7; European Economic Community, 1958, p. 48.
43. Holloway, 1981, p. 16.
44. Ibid., 1981, p. 20.
45. Collins, 1975a,b.
46. Holloway, 1981, passim.
47. Collins, 1975b, p. 235.
48. Holloway, 1981, p. 32.
49. Ibid., p. 17.
50. Collins, 1975b, pp. 220ff.
51. Holloway, 1981, Part II.
52. Collins, 1983.
53. Lipsey and Smith, 1986b, p. vi.
54. Ibid., pp. vi- xii.
55. Van Langendock, 1972.
56. George and Lawson, 1980, passim.

57. United States, 1986, passim.
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DISCUSSANTS

Gérald Pelletier

The trade deal will affect our personal and corporate taxes indirectly. The impact will occur through the lobbying pressures of the business class within Canada who, in the name of competition, will lobby to render our personal income tax system less progressive and to lower corporate tax rates. The downward pressure in taxes will, in turn, affect our social security system. We had an expanding welfare system in the 1960s and 1970s. It was part of a full employment strategy. It was part of a vision of how we saw Canada. It was also part and parcel of our ability or our willingness to tax individuals and to tax gains in our wealth in order to finance our social programs. In the future, we will be less able to increase taxation and government will be hard pressed to finance our social security system or even to keep our current social security measures.

Another reason our social security will be in danger is that the free trade deal is not only about a reduction in tariffs, but also about what the government can do to create full employment. We don't know how the subsidy code will be defined. We don't know how the government will be able to develop our regions and our industry. As a result of the free trade deal, it is quite clear that government will be less able to use procurement policies to increase employment in Canada. As a result of the deal, it will not be possible to have performance guarantees on foreign investment to increase employment. If we cannot move toward a future where full employment is a possibility, our social security system will falter.

Todd Rutley

There are already certain pressures on government to harmonize policies. However, I do not think they will necessarily be increased or decreased by the free trade agreement. When I look at programs like Unemployment Insurance and Workers' Compensation, I know that employers' associations have called for their rationalization. At the same time, I have seen these programs become more generous over time, so I would suggest that business has not been terribly effective in having its agenda adopted in the past. I don't think that public values with regard to Workers' Compensation

or Unemployment Insurance will change, and I think that the public will is the determining force in public policy. It is what Canadians are willing to buy politically that counts. While business will try to exercise pressure on policies, just as all lobbyists do, pressure does not equal action.

I also think that Canadians are willing to support health care and education. Even conservative media like Time Magazine or the Wall Street Journal have, in recent years, talked about the lamentable state of American education. There is a renewed effort within the business community in Canada as well to increase spending and the quality of education. I see that coming from the Business Council on National Issues and from the Canadian Manufacturers' Association. Those programs and income security for the elderly generally have broad support in the business community.

Coming to the question of tax harmonization, arguments have been made that because of free trade, corporations will seek to reduce the tax burden they bear to become more competitive with the United States, and that, in turn, will decrease revenues for the government. If you look at the corporate sector, you find many areas where the corporate tax burden is comparable to the United States. That is the case in the more mobile manufacturing industries where the income tax rate in Ontario is a little bit lower than New York or California and a little bit higher than a few other states. Capital depreciation allowances aren't quite as attractive in Ontario but on the whole they are fairly competitive. In the small business sector, Canada's tax rates give us a vastly favourable regime to promote the growth of small businesses across the country. In the area of services, I believe that we are taxed at a slightly higher rate than the United States. Hence I do not see pressures being exercised on the public purse because of the free trade agreement.

The general problem which Canadian governments face at all levels seems to be the imbalance between revenues and expenditures. I think that with the deficits at the federal and provincial levels, all participants in the public policy process have to determine how we are going to be able to bring the expenditure and revenue equation into line through either expense reduction or tax increases. But once again, I do not see how that problem is dramatically changed by the free trade agreement.

Lise Poulin Simon

It is not so much the strategy of free trade which represents a danger to Canadian social policies. It is the fact that the free trade agreement is not accompanied by other economic initiatives. Failures to correct regional imbalances and to solve the unemployment problems of Canada have made laissez-faire economic policies and the reduction of the welfare state attractive to some segments of the population. As long as monetary policies are only geared to full employment in Ontario, social policies will be vulnerable.

To the extent that we are unable to establish economic priorities and to elaborate strategies which reconcile social and economic interests and favor all regions of the country through employment expansion, social policies will be weakened. Trade barriers are never adequate to protect social programs.

The evidence from countries like Austria, Sweden and Norway suggests that it is not so much free trade agreements which harmonize social programs but the presence of corporatist institutional structures. These countries clearly favor free trade but also have strong social policies because they integrate social and economic priorities through full employment initiatives. In this respect, it also is important to note that it is not the centralization of economic policy in the hands of government which have favored the expansion of social programs but the democratization of political and economic decision-making.

A policy of full employment allows for public intervention which is consistent with a free trade agreement. An example is regional development. The logic of the market leads to inequalities in regional development. While the free trade agreement will not permit government to provide subsidies which directly affect commercial exchanges, it is possible to establish support which is indirect, focused on human capital. Regional industrial promotion, for example, is acceptable under free trade if it is addressed to improvements in human resources through research or management or adjustment rather than physical assets. Similar distinctions can be made with respect to government procurement and investment.

Brian Powell

I do not think that we have to worry overly with respect to the harmonization issue. When I looked at the Caribbean Free Trade Association and the Latin American Free Trade Association several years ago, I concluded that they failed because there was insufficient harmonization of social and political objectives. In the Canada-U.S. Free Trade Agreement, we are now worried about increased harmonization. Hence, when I reflect on these contrasting initiatives, I believe that when countries come together in free trade negotiations some threshold of harmonization of social objectives must be achieved. Secondly, I am impressed at how difficult it is to obtain harmonization of social policies even within one country. The federal government has not been very successful at fostering interprovincial harmonization. I think the extensive harmonization of American and Canadian social policies will be very difficult to achieve. Nevertheless, I also think that almost by definition, we are going to need a change in social policies as a result of free trade. Whichever side of the fence one is on with respect to free trade, there are winners and losers. Hence, what we need to do rather than talk about whether we will become more or less like the Americans, is to identify the specific issues and what we should do about them.

CANADIAN AND AMERICAN INCOME SECURITY RESPONSES TO FIVE MAJOR RISKS: A COMPARISON

Dennis Guest

All advanced industrial societies recognize and make provisions for certain contingencies which affect broad segments of the population: old age, invalidity or death, sickness and disability, work-related injury, unemployment, and the costs of medical care and of raising a family. In one way or another, all industrialized nations have had to formulate policy in response to these and other risks to income security. Without knowing otherwise, a considerable degree of homogeneity might be expected of American and Canadian social programs given the commonalities of historical antecedents, language, economic development and custom. In fact, the differences are quite striking.

While the Canada-U.S. Free Trade Agreement (CUSFTA) negotiations were in progress, Canadian government officials, on more than one occasion, emphatically stated that social programs were not part of the negotiations. The Americans, however, took a somewhat different view. Peter Murphy, the American negotiator, was reported in the press as saying that "everything is on the negotiating table including social programs." He later amended this statement with the qualification, "trade-related social programs." Comments such as these have contributed to a sense of unease among some Canadians that their social programs could be challenged in the future as an irritant or impediment to free trade, or as an unfair subsidy by government of a business sector's labour costs.

The object of this paper, then, is to compare Canadian and American security provisions in response to five major risks. An effort will be made to identify the significant variations in policy and program which might become the subject of harmonization pressures sometime in the future.

General Observations

The American social security system was launched during the Great Depression when social insurance protection against unemployment and old age was instituted in 1935. In addition, a number of federally assisted measures of public assistance for such groups as one-parent families, the elderly and the blind were begun. If the Americans were first off the mark, their pace of development has been erratic compared to the slow but steady developments in Canada. Furthermore, American efforts have been directed at categories of needy people, while Canada adopted more of the European tradition of providing protection on a universal basis. Health care, family allowances and a basic old age pension are examples. Americans have no universal programs.

Both the Canadian and the American income security systems are categorial in the sense that they attempt to differentiate between people who are not expected to work and those who are. In both countries, the elderly, the disabled and single parents with young children generally fall into the first category, although the position of single mothers has been more ambiguous in this past decade. All other adult citizens are considered employable and are expected to honour the central role of work in our society and display a commitment to self-reliance. One result of this emphasis has been a long-standing recognition in both countries that their respective income security networks fail to support or supplement the incomes of the working poor. Michael Harrington, for example, regards the welfare state in the U.S. as primarily for people over 65[1]. The recent Macdonald Commission argued for more significant assistance to Canada's working poor. Despite these and other complaints, the Canadian social security system presents itself with much more authority as one system for all Canadians, whereas the American social security system appears bisected, with social insurance protection for a majority and a stigmatizing welfare system for a sizeable minority.

Both nations emphasize work-related benefits through compulsory social insurance schemes. From this standpoint, both systems reflect the "handmaiden model" of social policy as described by Richard Titmuss, a model which views the income security system as an adjunct of the economic system, designed to encourage productive work and effort by linking retirement, unemployment and other benefits to a long and stable

employment record. The Canadian income security system also has elements of what Titmuss called the "institutional redistributive" model of social policy, which regards social programs as major forces for social integration through the provision of universalist services unrelated to any test of financial need.[2]

Having elements of these two models in the Canadian situation means that Canada's income security programs display a greater variety of income support techniques. On the basis of financial eligibility, for example, four types of programs can be identified: demogrant, social insurance, income-tested benefits, and means or needs-tested benefits. The American system has essentially two: social insurance, which comprises nearly three-quarters of total income support expenditures, with most of the balance delivered through welfare type programs on a strict means-test basis.[3] In Canada, on the other hand, using 1984-85 figures, social insurance delivers about 43% of income support benefits, demogrants just over 25%, income-tested benefits 10.7% and means-tested benefits 12.6%.[4]

Income security programs in the U.S. and Canada have been the object of numerous government studies and commissions over the past two decades. Ideas for reform developed in one of two general directions. In the 1960's and early 1970's, in both countries, the question posed by those reviewing income security was one concerned with social equality: "What does it do for the poor?" In the 1980's, the question being asked is more concerned with economic efficiency: "What does it do for the stability and growth of the economy?"[5] In both countries, over the past two decades, efforts at extensive reform of the income security network have been proposed but not carried through.

Comparing Income Security

In reviewing the income security programs of Canada and the U.S. in a comparative way, it is necessary to first classify the more than 100 major Canadian programs and the over 40 separate programs in the U.S.A. One useful means of classification is to separate the programs acording to the eligibility criteria employed. Thus, demogrants are payments made to certain categories of the population, generally on the basis of age and without reference to their financial situation; social assistance benefits require an income test or a means test; and social insurance provides wage-related and/or flat rate benefits to those with a work record in

covered employment. American income support programs can be broadly classified into two categories: social insurance, and social assistance (or to use the American term, welfare, that is, income-tested or means-tested programs). When reviewing American programs it is also useful to keep in mind the distinction between benefits in cash and benefits-in-kind.

Old Age, Survivors and Invalidity

The Old Age, Survivors and Disability Insurance (OASDI) program in the United States covers 95% of jobs and provides wage-related retirement and disability pensions, including provision for dependents and survivors of insured workers. A health insurance package was added in 1965, comprising a mandatory hospital insurance plan and a voluntary plan for physicians' services. The program is financed on a pay-as-you-go system, with a payroll tax on employees and employers of 7.51% each on earnings up to a maximum of $43,800 (1987) while the self-employed pay 13.02% (1988).

The Canada and Quebec Pension Plan covers 95% of the labour force and is a partially funded plan financed by a 2% tax on maximum pensionable contributions of $26,500 (1988) paid by employee and employer, while self-employed people pay 4%. Wage-related retirement, survivor and disability pensions are provided, but unlike the American plan, the C/QPP does not carry any additional costs for medical or hospital care as these are covered by the universal health care plan. However, UI benefits in Canada are an additional charge of $2.35 per $100 of weekly insurable earnings for employees, and 1.4 times that rate for employers.

Maximum retirement benefits under OASDI are $822 per month in 1988, which approximates the Primary Insurance Amount (PIA) that is the base for computing all types of benefits payable on one individual's earning record. Thus, the 65 year old dependant wife of an American retiree receives a benefit of 50% of her husband's PIA, thereby providing this couple with a total benefit of $1233 per month in 1988. A similar couple under the C/QPP, both sixty-five and assuming that one spouse is not in the labour force, would be eligible for a maximum benefit of $543 (December 1987), plus each would receive the Old Age Security demogrant of $310.66, thereby providing a total income of $1164.32.

An American widow of 65 drawing a survivor's benefit in 1988 would be eligible for 100% of her husband's PIA, which at the maximum rate would mean a widow's pension of $822 per month. A Canadian widow of 65 in similar circumstances would be eligible for 60% of her husband's C/QPP pension, or $325 plus her OAS demogrant of $310.66, providing a total income of $635.66 per month. However, the Canadian widow would also easily qualify for an income-tested Guaranteed Income Supplement of $206.66 per month, bringing her income to $842.32. In both of the foregoing examples, quite comparable benefits are received.

However, only a minority of beneficiaries under both plans draw maximum benefits. In the U.S.A. in 1988, while the maximum retirement pension payable is $822 per month, the average retirement benefit paid is $513. Very low pension benefits in the U.S.A. can be supplemented by a means-tested program called Supplemental Security Income (SSI), which in 1986 paid an average benefit of $228 per month. However, in 1984 only 5.6% of OASDI beneficiaries were in receipt of SSI, vivid testimony to the strict means-test applied. This contrasts in 1984 with the average Canadian wage earner who received the maximum C/QPP pension ($387.50 a month) and still easily qualified for more than $1,300 annually in GIS benefits.[6]

Average monthly benefits under OASDI for children of retired workers ($196), of deceased workers ($330), and of disabled workers ($142) in 1985, appear considerably better than the flat rate for orphans' and childrens' benefits provided under the C/QPP of $87.56 per month, even though this amount was improved by the universal family allowance of $31.27, for a total of $118.83. This amount could be further improved by the refundable child tax credit, which in 1985 paid a benefit of $367 or $30.58 per month per child, available to all families with a net annual family income of $26,330 and reduced for incomes over that amount by 5 cents for every dollar of additional income. Furthermore, Canadian child dependent benefits under C/QPP are paid to every child in the family with no family maximum. Under OASDI there is a family maximum, a figure which varies between 150% and 188% of the PIA, which means that benefits are reduced for each child dependent when the maximum figure is reached.

Changes have been made recently in the OASDI benefit formula which will mean that in all future years, the retirement benefit is expected to replace about 41% of

prior covered earnings for persons who worked a full worklife at earnings equal to the average in the economy and who retired at the full benefit retirement age.[7] For people working at the federal minimum wage, the replacement rate will be about 57%. For higher income persons who always earned the maximum, subject to social security taxes, the replacement rate will be about 27%.[8] The C/QPP in 1984 replaced 20% of average industrial earnings and 25% of insurable earnings. But according to Leonard Shifrin, the combination of C/QPP and OAS/GIS benefits means that Canadian workers in high, medium and minimum wage categories will draw a more adequate retirement pension than their American counterparts.[9]

Other elements of the American program that distinguish it from the Canadian program are the pensionable earnings amount on which payroll taxes are levied -- $43,800 for OASDI in 1987 and a tax of 7.51%, contrasted with a maximum pensionable earnings amount of $26,500 (1988) and a tax of 2% for the C/QPP. The American plan will, by the year 2022, increase the normal retirement age to 67 from 65. It will still be possible to draw a pension at age 62, but the reduction in benefits will be greater than it is today. No similar policy has yet been proposed for the C/QPP. A greater variety of beneficiaries are eligible for benefits under OASDI than under C/QPP. For example, a retired worker may also receive benefits on behalf of: a dependent spouse age 65 (reduced benefits paid at 62); dependent grandchildren; a dependent child or grandchild if disabled before the age of 22; or a wife of any age caring for an entitled child who is under 16 or disabled.

Sickness and Maternity

In the United States, there are two major public programs: Medicare and Medicaid. Medicare provides health care primarily for the aged within a framework of social insurance, while Medicaid provides health care for the poor within a framework of public assistance.[10] The latter framework is so rigidly defined and has been the subject of such cutbacks in the past decade that approximately 60% of American poor are ineligible for its help.

The Medicare program was enacted in 1965 to cover the medical expenses of the elderly as part of the OASDI social insurance package. It is comprised of two parts: Hospital Insurance (HI) financed by the social security

tax; and Supplemental Medical Insurance (SMI) to cover physicians' services, financed by a combination of voluntary premiums and federal general revenues. Because Medicare is seen as part of a social insurance program it might be viewed as analogous to the Canadian Medicare program. However, the American plan is replete with deductible payments and forms of co-insurance that Canadians have largely banished from their plan. In 1988, for example, the HI deductible rises to $540 (from $520) for benefit periods beginning in 1988. After the deductible has been satisfied, Medicare pays for all remaining covered services during the first sixty days, all but $135 a day (up from $130) for the sixty-first through the ninetieth day, and $370 a day (up from $260) for lifetime reserve days. For post-hospital stays in a skilled nursing facility, Medicare pays in full for covered services during the first twenty days, and for all but $67.50 a day (up from $64) for the twenty-first through the hundredth day. The basic premium for SMI in 1988 will be $24.80 a month.[11]

In Canada the Medicare program covers a comprehensive range of hospital, medical and pharmaceutical costs, financed in seven of ten provinces by general revenues, and in the other three and the Yukon, by a combination of individual and family premiums and general tax revenues. As the National Council of Welfare has pointed out, health premiums are a regressive, inequitable and inefficient form of taxation. Premium assistance is available and low income people with no taxable income are generally exempt, as are the elderly (except in B.C.).[12] Canada's overall performance in the health care field seems demonstrably better than its U.S. counterpart. As the Economic Council of Canada recently reported, Canadians enjoy a higher life expectancy and lower infant mortality. Health care costs -- including both public and private spending -- are about one-third more in the United States than in Canada.[13]

In view of the expected free trade in services that will follow from the CUSFTA, Canadians may wish to reflect on the fact that in the United States, proprietary chains own or manage a growing number, but still a minority, of hospitals -- approximately one-eighth to one-fifth of the total. Under the free market ethos which they have helped to engender, even non-profit hospitals are encouraged "to view their activities as a series of product lines with varying rates of return..."[14] A change in the management culture is also noted in American hospitals. The professional background of administrators has shifted

from public health to business administration, which to some observers, helps to erode whatever commitment to community service hospitals once had.

Because health care costs escalated sharply following the introduction of Medicare and Medicaid in 1965, state and federal governments, as well as private insurance companies (whose costs also dramatically increased) have experimented with various ways of controlling high cost sectors such as hospital care and fee-for-service. Alternatives to hospital care such as Community Health Centres and Health Maintenance Organizations are developing with favourable results from a cost and quality-of-care point of view. Interest in capitation plans for doctors' services is growing and being encouraged by Medicare. The Americans also use the forces of the marketplace to bring down per diem hospital costs, by permitting private insurance companies to bargain aggressively with hospitals to bring down the costs of caring for insured patients. This has given hospitals less leeway to treat "uninsured" cases, i.e., the poor, leading to a denial of services to that group.[15]

American proprietary hospitals and management services may well move into Canada, offering cost containment ideas as well as a range of marketing ploys for financially pressed hospitals. The American experience with these systems will have to be carefully scrutinized to avoid the biases which tend toward 'cream-skimming' in the interests of profitability.

Maternity Benefits

A unique aspect of American social policy is that country's reliance on the private sector to provide the bulk of income and other protections to working women during pregnancy. There is no statutory national maternity benefit in the U.S. as there is in Canada under the UI system. Five states and Puerto Rico have legislated Temporary Disability Insurance laws which cover maternity in the same way as any other disability. The American federal government also provides maternity benefits for its employees. Apart from these programs, American women in the labour force must rely on their employer and/or their union to provide a benefit package which includes maternity benefits. As a result of the Pregnancy Discrimination Act passed in 1978, which amended the 1974 Civil Rights Act, any employer who offers non-work-related temporary sickness or disability benefits must cover maternity to avoid a charge of sex

discrimination. This act does not apply to businesses with fewer than 15 employees and 20% of all employees work in such companies.

Three fundamentals of maternity policy are: health insurance covering hospital and physician's services, including pre-natal and post-natal care; a job-protected leave; and, full or partial wage replacement.[16] The United States falls far short of these standards. Employers in the U.S. are not required to provide for short-term, non-work-related sickness or disability, although in 1983 almost two-thirds of wage and salary workers were protected by a formal plan for such exigencies. The extent of protection in the U.S. is not well documented -- that in itself is an indication of the disjointed nature of public policy in this area--and some estimates suggest that as many as 60% of American working women may be unprotected. Maternity leave of 8-12 weeks is customary, with hospital and other medical benefits sometimes included, but compensation for wage loss is much less common.[17]

In Canada, wage loss for maternity is compensated for with 15 weeks at the same level as UI benefits (60% of the worker's usual wage) after an initial two week waiting period. Once again there is a considerable difference between maximum benefits payable ($276 a week in 1985) and average benefits paid. Monica Townson reports that in 1983, average maternity weekly benefits were $169 or 73% of the maximum available ($231) in that year.[18]

The qualifying period for maternity benefits is 20 weeks of work in the past 52-week period. This is a higher qualification than is demanded of unemployment insurance claimants in areas of high unemployment. Despite the appearance that Canadian working women have access to maternity benefits, rigidities in eligibility conditions have meant that many applicants have not qualified. Since January 1, 1984, some of these rigidites have been addressed. A take-up rate that was formerly 45% has risen to between 50 and 55%. Benefits are also available to adoptive parents, mother or father, and most recently to natural fathers. Some Canadian labour unions have included provisions in their collective bargaining agreements which provide fully paid maternity leave and for extended periods.[19] Some employers have developed similar plans for highly paid female employees.

Supplementary Security Income (SSI)

Any aged, blind or disabled person in the U.S. whose resources are currently less than $1800 (single) or $2700 (couple), excluding a home, personal effects of a reasonable nature, a car worth less than $4500 and insurance policies with a face value of $1500 or less, is able to pass the asset test for SSI. The guarantee level, as of January 1987, was $340 per month for an individual and $510 for a couple. The first $20 monthly in OASDI benefits or other earned or unearned income is not counted. However, unearned income above this amount is deducted dollar for dollar. Also disregarded is $65 of monthly earnings plus one-half of any earnings above $65. States may supplement this federal allowance and about half do so in widely varying amounts. Benefits are adjusted annually to the cost-of-living.[20] "Harrassment, indignities and bureaucratic red tape reminiscent of other means-tested programs are characteristic of the administration of SSI in many jurisdictions."[21]

In December 1987, the guaranteed income floor for elderly, low income people in Canada through the OAS/GIS combination was $785.31 for a couple and $674.47 for a single pensioner. Every two dollars of additional income reduces the guaranteed supplement one dollar and the benefits are indexed to the cost-of-living quarterly.

Sickness Benefits

Compensation for lost wages due to short-term sickness or disability which is not work-related is available to Canadians under the UI program of Special Benefits. With a medical certificate, claimants may receive up to 15 weeks of sickness benefits at the same replacement rate of 60% of average weekly insurable earnings. Some employers provide sick leave with full wage replacement for short spells of sickness. In the United States, only five states, Puerto Rico and the railroad industry have Temporary Disability Insurance legislation, which partially compensates workers for lost wages caused by temporary illness or disability. All other employees must either make their own arrangements or depend on union-negotiated or employer-initiated insurance or sick leave plans. Through these various means, in 1983, an average of 36% of the estimated income lost through temporary sickness or disability was replaced. Workers in private sector jobs not covered by Temporary Disability Insurance legislation averaged only 23% replacement of lost wages whereas government workers averaged 84%.[22]

Work Injury

Workers' Compensation, designed to provide cash benefits and medical care for people injured while at work, is the oldest form of social insurance in both the United States and Canada, dating from the World War I era.[23]

In the United States in 1985, a total of 55 state and federal workers' compensation laws covered 87% of the employed wage and salary labour force. Occupations not usually covered are domestic service, agricultural employment and casual labour, although even in these areas, 37 programs offer some protection for agricultural workers and 25 programs cover domestic workers. Employers in most jurisdictions are permitted to use commercial insurance companies to insure liability against work accidents. In eight jurisdictions commercial insurance is prohibited. State insurance is available in four of these jurisdictions and a choice between state insurance or self-insurance by employers is available in the remainder. In Canada, each province has established an autonomous agency responsible for administering its Workers' Compensation Act, and 70 to 90% of the labour force, depending on the jurisdiction, is insured for wage loss and medical care for work-related injury, disease or death.

Compensation payments for both temporary and permanent disability in American state programs aim at replacing approximately 66% of insurable earnings. In Canada, the replacement rate in similar circumstances appears to be higher -- 75% of insurable earnings, and in some jurisdictions, 90% of net earnings up to the maximum insurable. Waiting periods in the U.S. range from two to seven days with a seven day period being most common. Waiting periods in Canada are less onerous with three provinces having no waiting period while the others have one to three days.

Workers' compensation schemes in the U.S. are almost exclusively financed by employers, except in a few states where employees are required to contribute toward the costs of hospital and medical care. The cost to an individual employer depends on the degree of risk involved in the particular industry and the "experience rating" of injury, death or disease. Labour critics of Workers' Compensation in Canada point out that more interest has been shown in keeping the assessment on employers as low as possible, with less interest being paid to the health and safety of the worker.[24] The cost

of this program to the employer, relative to other labour costs, is small. One study estimated that workers' compensation assessments represent approximately 1.5 points out of a total employer labour cost of 132.3 points.[25]

Unemployment

The Economic Council of Canada noted in its Annual Review for 1987 that the Canadian UI system is more comprehensive and relatively more generous than the American system.[26] This response is explained by the fact that Canada is subject to higher rates of unemployment brought on, in part, by seasonal extremes and the importance of its primary industries. The attributes of the Canadian program are also one of the consequences of being a national system. The American UI program, by contrast, was established at the state level from the beginning to avoid the possibility of a system of national benefits undermining local labour markets.[27] An additional reason for the differences in the two systems may be the use of the "experience rating" in the United States.

Experience rating gives a business or industry an incentive, in the form of reduced UI payroll taxes, to stabilize its labour force by reduced working hours rather than by lay offs. It also serves to allocate the cost of UI benefits among employers in accordance with their presumed responsibility for causing unemployment. An eminent authority in the American social security field has noted:

> This approach to unemployment insurance inevitably leads to efforts to prevent the employers' accounts (which greatly influence the rate of tax payable by the individual employer or employers as a group) from being debited with the cost of benefits paid to their ex-employees. It explains the pressure for long periods of disqualification and for provisions which cancel all benefit rights as a result of voluntary quitting, discharge for misconduct, or refusal of suitable work. As we have seen, however, such provisions can seriously impair the income maintenance objectives of the program.[28]

It is arguable that experience rating has operated to reduce UI benefits and to restrict eligibility. In this context, the Economic Council of Canada's Annual Review notes that the number of unemployed receiving UI

benefits in the United States is "extraordinarily low" - only one out of four. In Canada, by contrast, almost 85% of the unemployed receive benefits. Some American authorities have reported a higher proportion of UI claimants, one that hovered between 45% and 55% through the 1950s and 1960s, reached a peak of 78% in 1975, but fell to 43% by 1982. The decrease is said to be due to changes in eligibility rules for extended benefits in a time of high unemployment and the length of time extended benefits are available.[29] While the Canadian UI system replaces 60% of insurable earnings, in the three years from 1982 to 1984, those Americans who qualified for UI received an average benefit, as a percentage of weekly wages, of 37.6%, 35.8% and 35.3% respectively.[30]

Because the Canadian UI system is more generous and comprehensive than the American system, it is therefore more expensive to finance and its costs are built into the Canadian cost structure to the possible disadvantage of Canada's competitive position with the United States. The Economic Council of Canada suggests, somewhat tongue-in-cheek, that Canada might have a case for launching a countervailing suit against the U.S. in view of the parsimonious UI system of that country.[31]

Poverty Related to Family Size

In Canada, a system of family allowances currently paying benefits to 6.6 million children is in place, and in January 1988, will provide $31.93 per month in most provinces and territories. Provinces may vary the amount of Family Allowance that the federal government pays to their residents according to the age and/or number of children in the family, and two have done so. In addition, the refundable Child Tax Credit initiated in 1978 as a supplement to the Family Allowance, will provide up to $489 per child for the 1987 taxation year, depending upon family income. The credit will rise to $559, effective the 1988 taxation year. Parents with a combined income of less than $24,000 will receive the full amount of the credit and additional income over that amount will reduce the credit by 5 cents for each additional dollar of income.

The United States does not have a system of family allowances but since 1975, it has had a restricted system of refundable child tax credits directed at working poor families. While the Canadian tax credit pays $489 per child in the 1987 taxation year, the American plan pays a stipulated sum per family.

Furthermore, the American scheme only provides a benefit to a family that has **earned** income, thus depriving families with an unemployed or unemployable head of the benefit. The Canadian plan pays benefits to all families of low or moderate income. The American Earned Income Tax Credit in the 1988 taxation year will pay a maximum benefit of $659 per family to families with earned incomes of less than $8,500. The credit is reduced by 10 cents for each additional dollar of earned income, with the cut-off point at $15,432.

Three other American welfare programs should be commented on even though they respond only indirectly to the risk of poverty associated with family size. These include Aid to Families with Dependent Children (AFDC), Food Stamps and General Assistance.

AFDC is a social assistance program established in 1935 and administered through state and local agencies within broad federal regulations and guidelines. It is jointly financed by state and federal funds, and in some jurisdictions with local funds as well. Depending on the economic resources of the state, the federal share ranges from 50 to 83%. The administration and delivery of this program's benefits bear a strong resemblance to provincial social assistance programs which are also cost-shared with the Canadian federal government. Although the provincial programs are not as narrowly categorial as AFDC, the caseloads tend to be dominated by single-parent families. If one is looking for program similarities between Canada and the United States, they are likely to be found in AFDC and provincial social assistance programs.

While not designed specifically for families, many have been helped by the Food Stamp Program which began in the 1960s and was greatly expanded in the early 1970s. To qualify, a household must have less than $1500 in disposable assets ($3000 if one member is 60 or older and the household has at least two persons) and gross income below 130% of the Office of Management and Budget poverty guidelines. (In 1984, the guideline figure for a four-person family was $10,220.) In making this calculation, some income is disregarded to acknowledge work expenses, child care expenses while parents look for work, and so on. Despite an 18% cutback by the Reagan administration, in 1984 over twenty million Americans received food stamps with an average monthly value of $42.77. The program's cost, financed by the federal government, came to $10.7 billion in that year.[32]

General assistance is "completely state-defined and state-local in financing." It provides help to those unable to qualify for major welfare programs such as UI and AFDC (which often does not accept families with two parents.) However, about one-third of the states refuse to provide general assistance to households containing an employable person, except in specific emergency situations such as fire or flood.[33]

Conclusion

In reviewing Canadian and American income security responses to five major risks, the matter can be summed up by referring to a comment by Harold Wilensky, who said that the three most important elements of social policy which differentiate welfare state leaders from welfare state laggards are health insurance, pensions and family allowances.[34] In all these three areas, Canada's provisions are superior to those available in the United States. This is one consequence of the American emphasis on economic individualism. Canada, on the other hand, has more of the European tradition of promoting equality through broadly based and universal programs. The question is, will Canada be able to maintain its social democratic tradition if tied more closely to the United States? This review of programs in five areas suggests that problems could develop as the result of a free trade agreement. The following problematic areas are suggested.

Unemployment Insurance

The American UI system employs "experience rating" which attempts to allocate the costs of UI benefits among employers in accordance with their responsibility for causing unemployment. The idea that an individual employer's insurance rates should reflect his risk experience would, if carried to its logical conclusion, oppose the socializing of any costs of unemployment. This is just one of the many examples of American handling of social insurance where the tendency is to emphasize the insurance aspect to the neglect of the social. Thus, extending UI to self-employed fishermen is an affront to insurance principles. Maternity benefits fall into somewhat the same category because many families plan on having children and insurance advocates would say that an income stoppage that is arranged is an inappropriate subject for insurance. Canada, having recently extended maternity benefits to adopting parents, seems to be giving more weight to the social argument. The emphasis on the insurance aspect leads to

an insistence that eligibility for, and duration of, UI benefits must be linked to an actuarially defensible attachment to the labour force. Thus, workers who stand most in need of protection -- casual labour, the seasonal worker and the long-term unemployed -- are excluded in order to uphold the insurance principle. This is the American pro-insurance approach, and one that has already been recommended for Canada by the Forget and Macdonald Commissions. Closer economic ties with the U.S. may well intensify a retreat from Canada's social goals.

Health Care

The Economic Council of Canada and Leonard Shifrin have both drawn attention to the difference in non-wage labour costs existing between the United States and Canada. A significant proportion of these costs for American employers is made up of private health insurance packages for their employees. Many Canadian employers also offer additional health benefits to their employees, but operating within the structure of universal medicare, these costs are considerably less.

American proprietary hospitals and management services covering such programs as temporary disability, sickness benefits and workers' compensation plans may move into Canada, offering cost containment ideas for financially pressed hospitals and for industries struggling to contain non-wage labour costs. These can be a source of contention if they introduce values that are foreign to Canadian tradition.

Pensions

The Canadian system of retirement pensions is more generous than that of the Americans, particularly when it comes to putting a floor under the incomes of the elderly. Because the OAS/GIS combination is financed out of general revenues and not by payroll deduction, Shifrin believes it could be the subject of a counter-vail suit, particularly for any U.S. industry that may be having trouble competing with its Canadian counterpart. The higher social security payroll tax in the United States could also become a point of friction.

Maternity/Parental Benefits

The hope that some have of extending maternity benefits into parental benefits with 75-90% reimbursement of wages and up to six months of leave may be even more difficult to obtain if Canada ties itself, in an economic sense, to a nation where the concept has such limited public recognition. Furthermore, any improvement in public programs for maternity benefits in Canada might be challenged as a subsidy to Canadian business (which indeed they would be).

On one aspect of social policy, the U.S. and Canadian societies have achieved a degree of uniformity. In both countries, female-headed families stand a good chance of living in poverty and in the absence of earned income, must turn to an inadequate and demeaning system of social assistance.

NOTES

1. Harrington, 1984, p. 85.
2. Titmuss, 1974, p. 31.
3. Garfinkel, 1982, p.13.
4. Government of Canada, 1986, p. 15.
5. Ozawa, 1982, p. 97.
6. National Council of Welfare, 1984.
7. Information on the Earned Income Tax Credit supplied by the U.S. Internal Revenue Service, Seattle, Washington.
8. U.S. Department of Health and Human Services, January 1986, p. 15.
9. Shifrin, 1987, p. 33.
10. Starr, 1986, p. 108.
11. U.S. Department of Health and Human Services, 1987, p. 2.
12. National Council of Welfare, 1982.
13. Economic Council of Canada, 1987, p. 51.
14. Starr, 1986, p. 128-129.
15. Ibid.
16. Kamerman, Kahn, and Kingston, 1983, p. 47.
17. Ibid., p. 157.

18. Townson, 1985.

19. Ibid., p. 35.

20. Information on SSI taken from the Social Security Bulletin, **Annual Statistical Supplement**, 1986.

21. National Association of Social Workers, 1985, p. 130.

22. Price, May 1986.

23. Information on Workers' Compensation in the United States taken from U.S. Department of Health and Human Services, vol. 49, no. 1, 1986, and Government of Canada, 1986.

24. Reasons, Ross, and Paterson, 1981.

25. Ibid., p. 172.

26. Economic Council of Canada, 1987, p. 49.

27. Garfinkel and McLanahan, 1986, p. 103.

28. Burns, 1956, pp. 165-171.

29. Blank and Blinder, 1986, p. 192.

30. **Statistical Abstract of the United States**, 1986, p. 362.

31. Economic Council of Canada, 1987, p. 51.

32. Harrington, 1984, p. 251.

33. **Social Security Programs in the United States**, p. 59.

34. Wilensky, **Income-Tested Transfer Programs**, p. 172.

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CANADA'S HEALTH SERVICES

George Tsalikis

Introduction

Several trade theorists have pointed out that free trade can have implications on social policy. They have particularly speculated on factors relating to harmonization of policies between the contracting countries, such as deviations from the average tax burden, the overall effect of taxation and a consensus about the desirability of specific social programs. Trade theory, however, has a limited scope and lacks an historical analysis of the relationship between nationalism, capitalist development and social policy, a topic largely neglected in all fields of social theory. This is why we cannot learn much from accounts of similarities and differences among cases of free trade and common markets, each of which has its own historical and geopolitical specificities. It is not possible to expand on such theoretical problems here, but their importance and complexity will be taken into account.

Since the publication of the Canada-U.S. Free Trade Agreement (CUSFTA) there has been a growing feeling of uncertainty about the future of Canada's social policies. The government's assurances that our social programs were not on the bargaining table and the urgency with which the deal was handled by both governments did not allow for a debate of the fears voiced by opponents of free trade. Aspects of health and social programs were, in fact, covered by the Agreement. Furthermore, the crucial question of what constitutes a 'subsidy' has been left to a future agreement, and it is feared that in the process, Canada will not have as much bargaining power as it had before the deal.

Some critics feel that an indication of the pressures to which Canada will be exposed once the CUSFTA is put into application can be seen from its concessions to the U.S. The United States emerged from the deal as the winner on many big points and the loser on fewer small ones.[1] Another ominous sign was the process established for the CUSFTA, which the NDP perceived as a "capitulation to the exigencies of the Legislative Timetable of the Americans."[2] There were many complaints about the lack of serious studies about the broader implications of the CUSFTA. There were also accusations that the government withheld information about negative sectoral and political implications of the deal.[3] Mistrust of the government was further fuelled by the mishandling of public hearings. The Standing Committee on External Affairs and International Trade of the House of Commons had to conduct public hearings across Canada in less than a month. Moreover, the hearings were concluded and the report of the Standing Committee issued before the text of the CUSFTA was made available.[4] For these reasons, several of the participants branded the whole affair with such terms as a "shotgun wedding", or a "kangaroo court."[5]

The expected consumer gains -- a greater selection of goods and services at lower prices -- may also be of questionable value when compared to the health status and social well-being of Canadians. As was pointed out by the National Anti-Poverty Organization, such gains could be accompanied by losses for the poor.[6] In a more general sense, the government and many advocates of the deal have argued that economic growth through free trade will secure, or further enhance, the development of social programs.

These contrasting arguments indicate how complex is the issue of harmonization of health services. There are the ambiguities involved in the concept itself. One difficulty is that harmonization denotes a qualitative adjustment of synergic parts, as is achieved in music. In this paper, it is used in a relative sense, referring to domestic institutional adjustments as a result of the implementation of a free trade agreement. To predict such adjustments, however, one must bear in mind the existing pressures in favour of harmonization. In this case they are particularly important due to the many common vestiges of the two countries and Canada's increasing economic dependence on the U.S. Another difficulty stems from the distinction between desirable and undesirable harmonization. In the following pages, the issue is discussed at two levels: national health

policy, and health care facilities. The discussion will also reach beyond the specific provisions of the CUSFTA to assess the effects of the agreement in combination with other forces. Therefore, three types of harmonization pressures will be examined: existing, CUSFTA-related and CUSFTA-specific.

National Health Policy

Many critics who raised the question of the impact of free trade on health policies, concentrated on the link between such policies and nationhood. As will be seen later, this is also true of the parallel critique of the Meech Lake Accord, which refers to the spending powers of the federal authority. A common perception in these debates is that health and other universal social and cultural policies are the pillars of Canadian identity, the basic elements of social cohesion that make Canada a distinct society from the U.S. Some critics also share assumptions about Canada's universal health policies which cause them to exaggerate differences between the two countries and underestimate the similarities. In doing so, these critics fail to see that harmonization has been going on since the decline of the British influence in Canada and the increasing American command over our economy.

Existing Pressures: The private-public insurance difference has masked several similarities between the two countries' health policies. The most important one is that both governments have been more concerned about the centralization of fiscal arrangements than with the development of comprehensive national health policies. Even the names of formulas developed for that purpose have been identical ('grants-in-aid', 'cost-sharing' and 'block funding'.) These arrangements were, in a broader sense, a compromise among governments, employers, popular demands and the medical industry, including hospitals and physicians. An unprecedented increase in medical technology, medical costs and premiums in the post-war years, coupled with an inability to collect bills, prompted governments in all industrial countries to introduce health insurance to distribute the burden over a broad public base. In North America, such fiscal arrangements were highly important to the medical industry because government was willing to pay, in full or in part, what the private purse could not buy. This was the case particularly in hospital care, the most costly sector, which lobbied for government intervention. Medicare insurance schemes covered mainly the diagnosis, and the patient paid privately for

whatever medicaments were required. Moreover, public support for the industry came with little control over safety standards, prices or considerations of effectiveness.

For these reasons, one can say that fears the CUSFTA will cause the end of medicare in Canada, or its replacement by the American mix of schemes, are an exaggeration. The policy has accommodated too many interests to be in jeopardy. Nor is it reasonable to support the long-standing expectation in both countries that the U.S. will harmonize its health policies with those of Canada. This was argued in the hearings before the Standing Committee, with reference to Canada's lower health expenditures per capita, lower overall administrative costs and larger population coverage. The powerful interests which profit best under the present American system were left out of the picture.

Although Canada's health policies are here to stay, there are reasonable fears that certain of its features will be negatively influenced by the CUSFTA, either directly or indirectly. Moreover, one can expect a decreased ability in this country to further develop polices in response to certain aspirations of the past two decades. To assess these assumptions, it is important to consider other common aspects of health care and trends to harmonization in the two countries.

First, a basic common characteristic that has persisted since the beginning is the decentralization of the administration of service delivery, including the negotiation of fees with medical associations. Decentralization was inevitable in both countries when the provision of medical care remained in the private sector and hospital care was provided by self-administered institutions that were financed or subsidized, directly or indirectly, by government. The same principle applied to the administration of public health and social services.

Second, soon after medicare was established in the two countries, fiscal reform began in the same direction. Its main purpose was to restrain the spiralling costs of health services caused by the introduction of these universal policies. This became the task of federal authorities on both sides of the border (due to the centralization of fiscal power.) The 'lifestyles' crusade paved the way for decisive federal shifts in both countries: direct or indirect cuts in federal funds for health care, and the transfer of fiscal and policy decisions to the second level of

government.[7] There were, of course, differences between the two countries in the scope of the new measures and their application. In the U.S., constraints hurt the poor more than in Canada and were accompanied by deregulation of federal health protection measures and the dismantling or amalgamation of categorial programs.[8] Mulroney's economic objectives -- paring the public sector in favour of the private one -- were largely in harmony with those of Reagan. However, due to the persistant popularity of the country's health plans (as shown by a Gallop poll in 1984) and growing worries about the Conservative's intentions, Jake Epp, Minister of Health, assured Parliament on November 23, 1984, that health care was 'a sacred trust' to be maintained. Fiscal harmonization continued in 1986. Mulroney's budget that year was designed to reduce federal transfers to the provinces for health care to achieve cumulative savings of $4 billion by 1991.

Third, the gradual passing of the political risks involved in fiscal constraints to the provinces was recently intensified by the Meech Lake Accord. This was perceived by many as the first step in the erosion of national policies, and by some, as the prelude to Canada's balkanization.[9] However, the general impression one gets from the literature on the Accord and on the CUSFTA is that they have not been put together under scrutiny. They may be like chemicals which, if mixed and exposed to some force, may explode and irreparably fragment Canada, the most decentralized federal state. Forces that are likely to cause such a series of detonations are also overlooked or misunderstood. They are all consequences of the major transformations associated with economic imperialism: the growth of multinationals; their increasing ability to transcend state controls; the resulting decline in nationalism as a force for capital accumulation; the growth of highly transient capital; and, the new international division of labour. Both fiscal constraints and the devolution of political risks are inevitable consequences of these transformations in the superstructure of a capitalist society. Most recent studies of the decentralization of the state show a tendency to harmonization at the centre. This results in increasing regional competition to attract investments, at a cost to social policies.[10] The fears of Canadian unionists about free trade are well grounded in this respect, and were recently put in the perspective of regional competition by Michael Lynk, a Canadian labour lawyer.[11]

CUSFTA-Related Pressures: So far, the discussion has been limited to general economic and political factors which are likely to influence harmonization tendencies in Canadian policy. To these will be added other forces which are not subject to the CUSFTA provisions, but which may be released as a result of the deal. Several submissions to the Standing Committee suggested that the CUSFTA links Canada to an ailing economy.[12] It was also argued that, because the U.S. now has lower overall rates of corporate taxation and much lighter taxes at the higher income levels, Canada will be forced to harmonize its tax laws and make them more regressive.[13] The fact that the Department of Finance has been comparing U.S. and Canadian tax rates for some years was seen as a sign of what is to come.[14] It is anticipated that tax harmonization could create pressures for the reduction and partial privatization of the 'sacred trust.' According to the Ontario Health Coalition, the CUSFTA holds our health care system (and other social programs) open to attack, through provisions that maintain each party's right to enforce or change existing domestic anti-dumping and countervailing duty laws.[15] The majority report of the Standing Committee did not directly address these fears about general forces which may combine as a result of the deal. It tended to stick to the letter of the Agreement and look to the future with only one eye. Thus it concluded:

> Some witnesses expressed the worry that the (CUSFTA) will set in motion a host of pressures to "harmonize" Canadian and American policies... in such fields as health care, employment benefits and government regulation. These are concerns that we would not dismiss lightly, but again ... the Agreement itself provides no grounds for such fears.[16]

The majority's position was that the Agreement is based on the principle of national treatment, which does not require a change in national laws towards harmonization, merely the same treatment for American and Canadian business enterprises in both countries, according to domestic law. This, of course, overlooks the possibility that domestic law can change under market pressures, in countervailing duty laws and otherwise. In this respect, the majority report rejected the fear that future definitions of subsidies will harm Canadian social policies and programs. The argument it presented, however, seems out of touch with the economic

and political realities described earlier. The issue of subsidies cannot be seen in isolation from the transnational accumulation of capital which financial provisions in the Agreement reinforce. The growing multinational market is characterized by complex formations that combine or accommodate the interests of other actors, to the detriment of those excluded from the exchange, mainly small business and low-income groups on both sides of the border.

Business and government interests frequently transcend state controls and national concerns. For example, the Canadian Life and Health Insurance Association, whose Canadian, American and European members already operate in a relatively free trade situation, supported the Agreement with one voice. Their aim was to eliminate rules on foreign ownership in order to "permit U.S. interests to purchase stock life insurance companies outright" and remove restraints on "commercial financial links".[17]

The majority also dealt with the problem of subsidies with reference to social programs in general. But what it perceived as "mutually exclusive arguments" in a general sense, are not necessarily so when it comes to programs which serve the needs of different social groups, or a specific program which serves different social groups disproportionately to their needs and according to their bargaining powers. Under pressure against a certain subsidy, government may 'take from Peter to give to Paul', especially if the latter's support, say for medicines, also serves a powerful monopoly covering both countries. Such situations would inhibit priorization of social expenditures according to the needs of those served in order to align them to market pressures.

A final point must be made about the argument from government critics that health care services should have been excluded from the deal. It is hard to see how this could have been done, except through an agreement on what constitutes a subsidy. The postponement of such an agreement made it possible to negotiate the deal within the allotted time. It is difficult to speculate on the repercussions of the postponement, but one cannot be optimistic given the anti-subsidy campaigns of American business. While it would be unreasonable to expect that the CUSFTA will force an overall harmonization of health policies, one should not "dismiss lightly" (as admitted by the majority in the Standing Committee), the fears about pressures to

harmonize set in motion by the deal. Such fears seem reasonable, not only in the absence of a definition of subsidies, but also in light of the two countries' common vestiges, essential policy trends, and Canada's increasing economic domination and political influence by the US. Pressures are also likely to result from additional fiscal constraints. Whether these are to be federal or regional, their effects can be expected to show at the provincial and institutional levels.

Health Care Facilities

Speculation about the harmonization of health policies as a result of free trade were reinforced by the fact that some aspects of health care facilities were covered by the CUSFTA. It seems this was not known, only suspected, before the Agreement was tabled in Parliament on December 11, 1987. Pat Carney, Minister for International Trade, assured Parliament on November 24, 1987, that "there is nothing in the... agreement that involves social programs...in any way at all." However, when the Agreement was tabled, Ed Broadbent, leader of the NDP, asked the Prime Minister to acknowledge that management services, virtually across the board in the health field, were included. Mulroney replied that the question was a matter of "legal opinion." Jake Epp, Minister of Health, argued in Parliament on February 4, 1988 that in this respect, the Agreement was "simply a recognition of the current way of doing things in Canada." He was referring to a handful of cases of private management which are not really representative of current practices but have raised fears about how things may be done in the future.

In fact, Broadbent's question in Parliament was an underestimate of what the Agreement actually covered. The understatement can be explained by the cryptic writing of the provisions of Chapter Fourteen. First, the services covered are presented in code numbers of the Standard Industrial Classification list. Second, 'health care facilities management' is listed in the Annex under Commercial Services. One can assume, therefore, that non-commercial services of this type are excluded. Third, the Agreement covers the management of all types of institutional and non-institutional services, such as hospitals, public health clinics, home-care services and 'homes' of any type for health and nursing care, community health centres, etc. Fourth, the management of offices of physicians, surgeons, dentists and chiropractors is covered. Fifth, the Agreement also covers services which do not appear

in the broad categories listed in the Annex: the management of institutional and non-institutional social services, as well as commercial laboratories. So far, there has been no formal reaction to these provisions by the Canadian Hospital Association or by other national organizations in the field. Other groups (e.g., the Pro-Canada Network and the Canadian Teachers' Federation), have already voiced their opposition. Before examining their concerns, however, it would be useful to give a brief account of existing practices, of studies on the effectiveness of private contract management, and of the desirability of such contracts.

Existing Pressures: Private management of public facilities has not demonstrated any considerable efficiency unless combined with norms that require a relaxation of public policies concerned with equity and quality of care. We shall follow, therefore, four broad avenues of privatization, identified in a recent study as the ones most debated from this viewpoint: increased use of private-for-profit management of hospitals; increased private funding of institutions; increased private funding of physician services through extra-billing; and, increased private funding of hospital services through user changes.[18]

Most forms of privatization have existed in Canada to some extent, but their increasing presence is largely attributed to American practices. Private-for-profit management of hospitals is not extensive in this country and is concentrated mainly in Ontario. It made its debut at Hawkesbury General Hospital, which contracted out its management functions to a subsidiary of American Medical International (AMI). Among the reasons the hospital board chose AMI were its management record of hospitals in thirteen countries and its assistance in obtaining a bank loan for the community's share of the construction of a new 'ultra-modern' hospital.[19] Contracting out the management of one or more departments followed in other Ontario hospitals (Peel Memorial, Carlingwood General, Toronto Wellesley, Marine Hospital, etc.).

Another debated case was that of Toronto-Queensway Hospital which contracted Extendicare to build and operate a chronic care unit. Even more controversial was a recent proposal of the Hospital Corporation of America to finance a large addition to the University Hospital

in London, Ontario, part of which was to be reserved for American patients. This caused a stir for several reasons. The corporation involved is the largest one in the field. It ranks 173rd in terms of sales and 166th in terms of profits in Forbe's list of the top five hundred. Moreover, the prospect of extra-billing and higher charges for American patients raised suspicions that they would enjoy preferential treatment as is the case elsewhere.[20] Outside Ontario there have been only a couple of cases of contract management -- in Alberta and Quebec -- but other provinces are looking into the matter with interest.

In response to the debate on privatization which followed the 'Hawkesbury experiment,' the federal Minister of Health commissioned two studies, one on management by private contract and one on the broader issue of privatization. The former concluded that "private management is no panacea" and that Canada could do much to change and strengthen the existing institutional management without changing its nature.[21] The other study saw no "optimistic estimates of the efficiency improving potential of private management."[22] It also warned hospitals against some negative consequences of U.S. private management, such as an altering of the service mix and discrimination against costly patients. The same views were recently expressed by the Ontario Federation of Labour in a brief to the Ontario Legislature's Select Committee on Health.[23] The Federation argued that the most important factor pushing hospitals in Ontario towards private management was access to capital. They also questioned the "success stories" about the Hawkesbury case, pointing out that the hospital's deficit was not removed by "superior management" but by a government grant. Only about 35% of the hospital's surplus can be regarded as "managerial in its origin." This resulted from staff reductions and room closures in the summer, but it represented only 2% of the hospital's budget and less than half of AMI's annual fee.[24] Finally, the Federation reached two conclusions. First, that hospitals, having lost a battle on arbitrated wages in 1974, subsequently sought marginal cost cuts through contracting out; and, second, that their gains from contracting out came primarily from a commercial strategy based on pricing policy, admission criteria, promotion of higher profit margin services and superior access to capital.

Apart from access to capital loans, some cases of private management of hospitals in the U.S. showed

surpluses only where two factors were present: a sufficiently large percentage of 'full pay' patients, and a policy that permitted charging such patients whatever was necessary to cover the hospital's deficit. This was shown in a study of seven county hospitals in California, which examined the situation before, during and after the contracting out of management.[25] The company's competence was not an important factor and the gains were not lasting. The study showed that the main contribution was in optimising reimbursement rates, a function that could be performed by county personnel or purchased from accounting firms at a lower cost. No clear-cut evidence was shown of cuts in operating costs.[26] It is not surprising, therefore, that of the six counties examined, two terminated the private contracts and returned to public management in the first phase of the study, and another two did so by the end of the study about two years later.[27] The two hospitals which continued under private management were small ones suffering from long-term management problems which the researchers thought were possible to resolve through a scheme of public management.

It is small, rural and neglected hospitals that seem most attractive to private management. Since the early seventies, the U.S. has seen small and medium private or public hospitals being purchased by profit and non-profit chains which combine management with financing and acquisitions; and this was made possible by means of government subsidies.[28] From 1974 to 1980, for-profit beds owned by investor chains grew from 49% to 95% partly through contract management, a complementary strategy designed for ownership and growth. A survey in 1986 showed a new tide of clustering through buying and selling of hospitals, the result of competition among commercial chains and non-profit 'multihealth' care systems.[29]

In Canada there has been no such 'tribal war' in the institutional sector, other than the traditional competition for government resources. Since the early seventies, cost containment has been achieved by global funding under which each hospital receives annually from the province a predetermined sum of money from which revenues for ancillary services are deducted. This began to change in recent years, through the gradual introduction of the 'business orientation new development plan' or BOND, the brainchild of hospitals in Rochester, New York. Ontario was the first province to adopt the plan as an administrative practice in 1980 and other provinces are now considering its

application. Under the scheme, the excess of revenue over expenses, achieved through cost reductions or through increased charges and new ventures, is not deducted from the hospital's budget. To achieve an excess of revenue, hospitals are encouraged to adopt the business practices of American hospitals, such as: differential rates for private and semi-private accommodation; increases in chronic-care charges, higher rates for preferred accommodation, and for non-residents of Canada or of the province; changes in the ratio of standard and preferred accommodation; new commercial ventures and higher prices for existing ones; hiring freezes, greater use of volunteers and stricter personnel policies; purchasing of commercial laboratory services; aggressive fund-raising, and many more. Some of these achievements of 'scientific management' seem to lead to a two-tier system which discriminates against 'costly' patients. Others have been criticized as a squeeze on hospital staff, on ordinary patients and their visitors.

An important question is who pays and who benefits? The latter is easy to answer by reference to the fact that many hospitals continue to expand their high technology to meet the demands of doctors in response to industrial growth.[30] As was concluded in one study conducted on behalf of the federal government:

> The evolution of health care delivery, has been characterized by the development of complementary, cost-increasing services rather than substitute, cost decreasing ones'.[31]

Much of this growth is achieved through BOND's sophisticated fund-raising and savings through volunteer time. A survey by the Ontario Hospital Association found that 125 of the 169 hospitals which responded raised $132 million in the fiscal year 1986/87, most of which, about $84 million, came from capital campaigns of 73 hospitals.[32] The hospitals covered had special fundraisers on staff. Generally, non-profit organizations in the health sector assisted the profit-making medical industry with an extra $672 million in solicited funds in 1980.[33]

Some of the regressive effects of a business orientation on the care of patients with different incomes have been pointed out in a review of the literature commissioned by the federal government.[34]

The effects of fund-raising for health care, a form of privatization or 'hidden taxation,' have not been studied. However, two general studies of charity support the assumption that the poor pay more as a result of fiscal constraints.[35] They showed that over the past fifteen years, the highest income groups have donated less and less of their disposable income, leaving a greater burden on both the elderly and the lower income groups to support non-profit organizations. Private corporations have shown the same attitude.[36]

There will be more emphasis on public fund-raising as hospitals enter a new period of fiscal constraint.[37] Hospitals may also have to increase the types of charges and the rates, and further reduce some supplies which have traditionally been provided to patients as part of total care. Moreover, extra billing may increase, despite its discouragement by the Health Act (1984), and may hit even patients on welfare, as has happened in Alberta.[38] It is inconceivable that physicians will be able, or willing, to do their own means tests. Generally, extra billing is a persistent aspiration of the medical profession.[39]

CUSFTA-Related and CUSFTA-Specific Pressures: A study on private management commissioned by the federal government suggested that:

> There is no significant support among Canadians for general "privatization" of their health care system... But private sector involvement in health care is acceptable in limited ways.[40]

It must be noted, however, that the acceptability and the extent of privatization vary across Canada. Many aspects of health care are open to extensive provincial variations which are bound to increase under the Meech Lake Accord. This is particularly true of management, which is basically left to provincial authorities, some of whom may feel increasingly inclined to try the American way under free trade. This concern was expressed in Parliament on February 4, 1988, by Don Ravis, a Conservative member who complained about the "already widely diverse method of health care management throughout the country." The Minister's response was that federal legislation "does not close the door on private sector management." It is hard to say at this point how wide the door will be open in different provinces. One of them, Alberta, has already shown signs

of a likely move towards private management beyond the level of service delivery. In 1984, it announced its intention to consider the transfer of certain provincial administrative functions to the private sector, and Price Waterhouse was commissioned to study the feasibility of the plan.[41] The project was shelved but it may return in the future when American multinationals increase their activity in Canada.

As for the issue of private management at the institutional level, studies commissioned by the federal government concluded that public administration can easily modify its practices to achieve, on a non-profit basis, marginal and short-term gains through private management. In this respect, the Ontario Federation of Labour argued that in the hospital sector:

> ...there already exists the expertise and the commitment to achieve greater technical efficiencies. Self reliance is always a superior basis for development than dependence on external, and especially foreign, sources.[42]

Such reasoning supports the optimists' belief that Canada will not rush to private management of health institutions, particularly since there is evidence of the marginal, short-term and otherwise questionable value of such practices on both sides of the border. However, if cost remains the dominant factor, as may well be the case under free trade, increased privatization of health institutions is likely to make private management attractive. This is the basis of its continuing growth in the U.S., through centralization and various combinations of interests and functions.

As was seen earlier, another argument expressed by advocates of free trade, in Parliament and elsewhere, is that services covered by the CUSFTA are already open to the private sector. Opponents of the deal, however, have pointed out that the list of services covered is not final. Thus, Article 1405 of the Agreement provides for the future implementation of services that are not now covered. Another fear stems from Article 1402(8) which does not require foreign firms to be located in this country in order to be treated like Canadian firms. The fact that they will be able to operate from the U.S. will make it easier for them to achieve cost reductions. It is likely that they will hire Canadian experts who know the institutional structures, procedures and

attitudes, and whose involvement will mitigate fears of Americanization. Moreover, the finance provisions will help them buy Canadian firms which are unable to compete. Generally, opponents to the deal anticipate that the provisions of the CUSFTA will enhance Canada's penetration by a few industrial giants in the field who combine management with other operations, to give them a competitive advantage in addition to their head-start in technology.

The climate which has so far prevented Canada from embracing private management of health facilities may also change under further fiscal constraints and reduced taxation capacity. Fiscal pressure can prompt a relaxation of government regulations on user charges, differential rates, and other aspects of care, which might make private management attractive at the cost of policy objectives. The door is already open to private management and deregulation. That is not an argument in favour of free trade in this sector, but rather an argument against it. The fear is that the door may be ripped from its hinges by an irreversible trend to economic and political harmonization forced by economic necessity. It is hard to predict how the public would react should this happen, and what effect this would have on political decisions. Opinion is already divided sharply over persistent concerns about quality and equity, despite evidence against the 'ultimate fix' of privatization. The recent debate of this matter in Quebec is instructive. Paul Gobeil, Treasury Minister (and a businessman), supported private management of certain hospitals on an experimental basis. Thérèse Lavoix-Roux, Minister of Health, reacted strongly against the 'miracle formula' of such management. The debate between the two, extensively covered by the media, caused such a division in cabinet that the Premier was forced to express his views. He was skeptical about the proposal on the grounds of quality, but he did not wish to adopt a 'doctrinaire' viewpoint by saying "jamais, jamais, jamais."[43] Even if he did so, no law would prevent him from changing his mind. "What is there to be lost by trying?"[44]

It is very likely that some provinces will begin experimenting with private management once the Agreement is in full force and the experiments, as we know from precedents, will not be comprehensive. Studies commissioned by the federal government advised that if private management were to play a role, the contract should bind it to public policy objectives. Under the Meech Lake Accord, such safeguards could vary from

province to province. Moreover, private management may accept binding contracts only to violate them in ways that escape government inspection, particularly in cases where the provincial authority would be primarily inspired by fiscal considerations. So far, the CUSFTA provisions are limited to the private management of health facilities, and private hospitals cannot grow because private health insurance is not permitted by the provinces for services provided under government schemes. These factors may change in the future, however, if an arrangement is reached under Article 1405 of the Agreement, to expand the types of services subject to free trade. It is hard to speculate on the matter at this point, as such an exercise would require a complex assessment of the incentives for American investments in relation to Canadian incentives for deregulation following the implementation of the Agreement.

The inclusion of private management in the deal has also raised fears about a possible invasion of Canada by American firms which operate chains of nursing homes. Private investment of this type is prominent in Canada and is growing fast with the prospects of an aging population. Here again, speculation is difficult because the Agreement covers only one aspect of management and there are no obvious reasons why Canada would be forced to accept coverage of the whole sector under Article 1405.

More serious complications may arise from the coverage of private management of community-based and such non-institutional services as home care, extended care, community health centres and similar facilities. Under the CUSFTA, the provinces will be less able to justify, if they wish to do so, preferential treatment for community groups involved in the administration of such services. Such involvement is highly regarded in this country and is in agreement with the broad definition of primary care incorporated in the Alma Ata Declaration.

Finally, a question must be raised regarding the argument that the door to private management is already open, even without free trade. If this is so, why did the contracting members have to include this service in the Agreement and leave the door open for other services to come? Was the American negotiator so naive as to accept an empty little box with delight? As no reasonable answer comes forward from the free trade defenders, one may assume that both governments were

lobbied by American multinationals to cover this sector. It is doubtful that pressure was also exerted by their Canadian counterparts, who would hardly be competitive in the U.S., particularly now that big, non-profit chains are also growing fast.[45]

Concluding Remarks

The CUSFTA is not about complete harmonization. Total harmonization does not exist even within Canada, nor in the U.S., where health care policies and practices vary remarkably from state to state. The main concern is that existing trends to harmonization are likely to increase when many of the differences between the partners are put under the general pressure of free trade and the specific provisions of the Agreement. Moreover, the progression to harmonization will most likely follow the American path. This, in turn, reflects a broader phenomenon reshaping the world economy and the state in two directions: centralization of economic power and fiscal controls; and, decentralization of fiscal responsibilities, social policies and administration. CUSFTA and the Meech Lake Accord clearly express these two tendencies.

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DISCUSSANTS

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In discussions about the Agreement, there is a general affirmation that free trade and the market will lead to an efficient use of resources. I think that is a fundamental flaw. The analysis is based on the assumption that the free market, left to itself, will fully use our resources and that it will naturally tend to full employment. The fact is, historically, that capitalist societies, left to themselves, periodically tend toward stagnation and under-utilization of resources, both capital and human. The reason why there has been protectionism all through history is precisely because there is not a tendency toward full employment. The countries that wanted free trade and have developed the ideology of free trade have always been the dominant countries in the world economy. The countries that have accepted protectionism and resisted the free trade arguments have done so, I would suggest, because they have needed their political liberty, their national sovereignty, in order to establish their own priorities, protect their own industries, and ensure their social values as well as full employment.

Secondly, I think that the post-war prosperity we had, particularly up to the middle 1960s, was essentially linked to the welfare state and the very rapid growth of social services. In an economy which enjoyed very rapid gains and productivity in the manufacturing sector and also in the primary sector, there was additional income. This, in turn, generated additional capacity for consumption. That capacity for consumption was absorbed in part by the development of social services paid for by the state. The crisis that we have come to, in my opinion, is not an economic crisis. There is absolutely no reason why we couldn't continue developing additional social services as a way of absorbing the labour power released from our productive secondary sector, and as a means of maintaining consumption at a relatively high level.

The current crisis is essentially political. It is a new offensive on the part of the business community, which sees the areas of the economy in which it is allowed to make profits as continually being squeezed because we have considered certain areas of social services not legitimate for making profits. The whole thrust we are getting into now, and it's again a political thrust, is an attack on the Keynesian approach and on the welfare state. It is a contestation of the legitimacy of government in providing services.

It is important to spell out, as specifically as possible, the ways and means by which the CUSFTA will alter our policies and programs, and whether such alterations are regressive, progressive or a matter of indifference to Canadian social policy objectives and values. In this respect, the term 'harmonization' needs to be better defined. Harmonization of social policy arising out of the CUSFTA should be defined as, firstly, those changes in Canada's social policy brought about or compelled by and therefore attributable to the bilateral free trade agreement (i.e., which would not have occurred in the absence of the CUSFTA); secondly, the changes in Canada's social policies made in order to conform with or become less distinctive or different from the policies prevailing in the U.S.A.; thirdly, compelled changes which are deemed less desirable than those Canadians would have chosen in the absence of the CUSFTA. Too often, in the debate on the CUSFTA to date, the term 'harmonization' has been used much too loosely and sometimes refers to nothing more than similarities between one or another feature of social policies or programs in the two countries.

CUSFTA is not the main threat to the medicare system of Canada. Medicare is too well-entrenched, too popular with the public. Also, large segments of the medical profession would prefer Canada's medicare system over the corporatist approach to medical practice that is developing in the United States. Corporate interests in Canada are such that they are not likely to argue for change either. Nor is it likely that all or most of the provinces would so radically change their policies to compel the significant changes to medicare that might constitute its harmonization with the American way of covering its citizens against health care costs. While the meaning and application of subsidies to the corporate sector under the CUSFTA have yet to be worked out -- a matter of great significance in assessing the effects of the Agreement -- it can hardly be suggested that governments do not subsidize health care services in the United States. They do, pervasively and massively.

But medicare is not the whole of Canada's health care policy nor of its health care system. It should be remembered that there is an agenda for health policy that has yet to be finished or accomplished. The Royal Commission on Health Services in the 1960s spoke of a "Health Charter for Canadians" and called on Canadian

governments to provide massive programs increasing the coverage of health services over time. Medicare was to be just the first and most costly of the public initiatives. It now seems that the fulfillment of the Health Charter for Canadians is unlikely. The obstacles are the CUSFTA and the Meech Lake Accord. Both of these represent mutually reinforcing influences that will make the expansion and fulfillment of the 'welfare state' values embodied in the Health Charter for Canadians very difficult to achieve.

While the unfinished health policy agenda is likely a casualty of the CUSFTA and Meech Lake, the CUSFTA will also put pressure on existing policies and programs. Whether the CUSFTA would lead to a great expansion of private, for-profit management of our institutions and programs can only be a matter of speculation. No doubt there will be a growth in such practices. But will the growth be enough to cause us difficulties? In what ways? If so, is there anything our provincial governments can do to prevent such difficulties from occurring? It is this sort of exercise that those concerned with the effects of the CUSFTA on social policy must engage in. Indeed, it is the identification of the pressure points and threats to our social policies arising from the CUSFTA that is sorely needed. It is only then that we can start thinking about how to prevent undesirable harmonization (as defined above). In fact, the identification of threats or dangers and mitigating solutions should inform Canadian negotiators concerning the task of defining subsidies, which, as was mentioned earlier, remains to be done under the CUSFTA. What is suggested is that we should use the very concept of subsidy as our first line of defence against undue and unwarranted pressure for the harmonization of our social policy (assuming that the CUSFTA cannot or will not be scuttled).

There are many specific questions that will have to be addressed in order to obtain a comprehensive understanding of the implications of the CUSFTA for Canada's health care system. They include the effects of the Agreement on the dental care markets in Canada, on the nursing home industry, on the home care, extended care and community-based health services, on the pharmaceutical and biologicals industry, on the medical devices and supplies industry, on the health care data and information processing and storage industry, on the laboratory industry, and so on.

There is much need for further speculation and debate on this whole question -- and the sooner, the better. Recently, Mr. Adam Zimmerman, Chairman of Noranda Forest Inc. and Canadian Co-Chairman of the Canadian-American Committee, warned that there will be intense pressure on Canada to consolidate and conform with American policies and perspectives on our social policy. In return for access to the U.S. market, Sam Gibbons, Chairman of the House of Representatives foreign trade sub-committee, told Zimmerman that Canada should not do things "different up there." In Zimmerman's words, that attitude "may affect our tax policy, our social policy, all kinds of things" (Toronto Star, March 25). With such warnings coming from staunch supporters of the free trade agreement, there is an even more urgent and serious task for the opponents of the agreement to do all they can to safeguard health and social policies from attacks through the CUSFTA.

Wilfred Brown

Canadians have shown themselves strongly committed to the present, relatively high Canadian standards of social services in the areas of health care, income security and public education. The federal government has been forced to back down repeatedly in its attempts to undermine or erode the Canadian social contract. Notable among the areas in which there have been strategic retreats have been the attempts to undermine the principle of universality of social benefits, to de-index pensions, and to reform the unemployment insurance system. To proceed directly with these or similar initiatives would clearly threaten the political survival of the present federal government.

What cannot be done by direct political action, however, may be achieved, over a longer period of time, by market pressures forced on the Canadian society and economy by the CUSFTA and the process of policy harmonization which is an integral part of it. In fact, some of the strongest advocates of bilateral free trade with the United States, such as the Canada West Foundation, support it precisely because they feel that the market forces unleashed will force the reduction or elimination of Canada's generous social programs.

For public education, the most serious implication of the Canada-U.S. Free Trade Agreement (CUSFTA) will be the long-term pressure to conform to public policy choices in the United States, in order to keep the costs of government services in Canada competitive in the

continental marketplace. Specifically, publicly supported elementary and secondary school systems across Canada are likely to face increasing pressure to follow more closely their generally less adequately funded and less equitable U.S. counterparts. As well as affecting funding levels, this pressure could ultimately affect the goals, structure and operation of Canadian public school systems and the extent to which our schools promote distinctive goals for Canadians and a Canadian national identity.

Not only does Canada devote a higher proportion of national resources to education than does the United States (5.3 per cent of personal income to elementary and secondary education in 1984, compared to 3.7 per cent in the United States), these resources are more equitably distributed according to the educational needs of Canadian children, regardless of where children live in Canada and regardless of other circumstances that separate them. Greater equity in education is achieved among the Canadian provinces than among the American states, by means of superior federal-provincial revenue sharing and the federal equalization program in particular. Average spending per pupil is higher in Canada than in the U.S. (an average of $3,420 U.S. in Canada over the three years 1983-86 compared to $3,199 in the United States), and it is much more equally distributed. For example, in 1985-86, the province with the lowest level of spending per pupil spent 61 per cent of the amount spent by the highest spending province, while the corresponding figure in the United States was 42 per cent.

As well as the existence of greater interstate than interprovincial educational disparities, there is evidence of considerably greater inequality of educational funding within American states than within provinces, due largely to the greater reliance in the United States on local property taxes for education. For example, in 1983-84, provincial governments in Canada provided 69 per cent of funds for elementary and secondary education and only 24 per cent came from local taxation. In the United States, by contrast, state governments provided only 48 per cent of funds, and local taxation provided 45 per cent or nearly double the local share of school financing in Canada. In short, Canada does a much better job than the United States of distributing its financial and human resources for education in accordance with educational needs, and of distributing the burden of paying for education according to the financial ability of the entire nation

and of the provinces to pay, rather than relying on real property.

Implementation of the CUSFTA would create greater pressures than already exist on Canada's beleaguered cultural industries. Book publishing and public broadcasting agencies are already under serious pressure due to the inundation of American-made material, and austerity in government funding. For education, for teachers, and for children in the classroom, the most serious implications of free trade in cultural industries would be the reduced availability of distinctively Canadian learning materials and possibly the erosion of bilingualism in school systems across the country.

The impact of free trade is likely to be most immediate and direct on some of the school children in most communities and regions of the country, and on virtually all children in the 800 or so single industry locations during the transition or phase-in period of the Agreement. These effects may be beneficial or detrimental, depending on whether the parents involved work in industries and occupations which are winners or losers. For children of thousands of people likely to be adversely affected as a result of the CUSFTA during the ten-year transition period, there are likely to be major disruptions and even permanent setbacks in the educational process. While the federal government and other proponents of the Free Trade Agreement insist that the dislocation and losses of employment in some industries and in some regions of Canada will be more than offset by the growth of investment and employment in other industries and other regions, there is no convincing evidence of this. As well as the strong possibility that the economic advantages of the Agreement have been overstated, there is a strong possibility that the adjustment problems are being underestimated.

For elementary and secondary school teachers, the major long-term hazard arising from the CUSFTA will be the political and economic pressure to harmonize labour laws relating to public employees in general, and to teachers in particular. Because the framework of labour law in the United States is much less favourable to unions and, in particular, to public sector unions than it is in Canada, this will result in downward political pressure on the legal and institutional framework of public sector and teacher collective bargaining in Canada. The labour relations systems of Canada and the

United States have been on divergent paths for over a decade. The deunionization movement in the United States has drastically reduced union representation to 17 per cent of the U.S. labour force. By contrast, a stronger legislative and institutional base in Canada has helped organized labour maintain its representation at 39 per cent of the Canadian labour force and fostered the growth of strong public sector unions.

Despite the erosion of collective bargaining in several provinces in recent years, all teachers in public elementary and secondary school systems in Canada still have the right to bargain collectively for their terms and conditions of employment. In the United States, by contrast, only 33 states have collective bargaining legislation for teachers and other school employees. A number of states have laws which inhibit full and free collective bargaining for teachers and other public sector employees. There are laws prohibiting collective bargaining or even 'consultation' in six states; there are 'right to work' (anti-union) laws in thirteen states; and 'sunshine' laws which require bargaining sessions to be open to the general public in six states.

Ken Murdoch

Social programs are very much at issue in the pact which President Ronald Reagan has aptly described as a "new economic constitution for North America." How could anyone have ever thought otherwise? Even without explicit mention in the text of the Canada-U.S. Free Trade Agreement, they were always implicit. The reason is competition. Canadian business, in order to compete, wants a 'level playing field.' U.S. business, in order to compete, wants a level playing field too. And we all know that economic and social policy go hand-in-hand. Generally, the free trade debate around the relationship between the social and the economic has focused on the implications for medicare, unemployment insurance, and worker's compensation. But, there are also several social programs in Canada that are delivered through what is often referred to as the personal social services. The management of many of these services is listed in the Agreement.

The provisions of Chapter Fourteen apply to a range of management services including: general, rehabilitation, extended care, psychiatric and childrens' hospitals; homes for the physically disabled, mentally retarded, emotionally disturbed children,

children in need of protection, alcoholics, drug addicts, and single mothers; and, home care services, blood banks, blood laboratories, public health and radiological laboratories. In addition, non-institutional health services are mentioned. They include management services for ambulances, drug addiction and alcoholism treatment clinics, private practice nursing, occupational therapy, physiotherapy, community health centres, and even a list of offices of private practice professionals, including groups of registered social workers who provide professional counselling to individuals, families and groups.

Obviously, the long list of institutional health and social services has to do with clearing up a misunderstanding that American interests were not particularly welcome to provide management services to these institutional services in the past. The CUSFTA now indicates that the welcome mat is on our doorstep, if not the key to the whole house!

'National treatment' is a hallmark term in the Agreement. Let us be sure of what is written, since those voicing support for the Agreement suggest that all those opposed to the CUSFTA are misconstruing the import of the term. In short, Article 1402 in Chapter Fourteen on services says that each country shall accord to persons of the other country treatment no less favourable than that accorded in like circumstances to its own persons with respect to measures of the chapter. Provinces or states shall accord treatment no less favourable than the most favourable treatment by such provinces or states to their own persons in like circumstances. And, where treatment may be different (for prudential, fiduciary, health and safety, or consumer protection reasons), such different treatment is to be equivalent in effect to the treatment accorded to its persons for such reasons. Prior notification of such treatment must be given.

The principle of national treatment surely implies that if we want to make any changes in our health care or social service delivery systems in Canada, henceforth, American companies or interests can and must be accorded non-discriminatory access to any tendering process pertaining to management services. Provinces could retain discriminatory practices towards 'persons' from other provinces, but not to American 'persons' beyond that which might happen to be directed to resident provincial 'persons.' Key to this statement are changes in our health care or social service

delivery systems. Existing laws and practices are 'grand-fathered'; they are allowed to continue as is. But any new regulations for covered services will have to conform to the national treatment obligation.

Three issues arise with regard to 'national treatment.' First, the CUSFTA states that government-provided health, education, and social services are exempt from the chapter on services. That does not take into account the rapid pace in privatization of social services taking place across the country. Such privatization has various manifestations. Some social services are being turned into commercial ventures. Many are undergoing devolution to delivery through community-based, non-profit organizations. Deinstitutionalization is one movement spurring this on, initiated by both economic as well as philosophic motivations. Does not this devolution, where a new arms-length relationship exists between government and many service delivery agencies, take the service out of the exemption of the CUSFTA?

Secondly, the principle of national treatment moves provinces somewhat out of the standards setting arena. They retain the right to set standards for services, accorded them by the Constitution and reinforced in spades through the Meech Lake Accord -- but, not if the standards discriminate against American parties. Provincial powers over health and social services will be within an international agreement where any stripping away of provincial power will not be to Ottawa, but rather to a trans-national setting. Remember, trade disputes will be taken up with a Trade Commission. That certainly puts the perennial power struggle between Ottawa and the provinces into a whole new perspective!

In the third place, if health and social services are privatized to the point of being commercialized, then the chapter of the CUSFTA on 'Investment' opens the door for direct social service delivery by U.S. firms in the marketplace.

The re-alignment and 'level playing field' implied in the services chapter of the CUSFTA now challenge the very tenets of that social policy stance fought for so diligently throughout Canadian history. It comes on the back of a growing movement in Canada about privatization of social programs and services. 'National treatment,' 'right of establishment' and 'harmonization,' when simply applied to management services within our social services, will have a direct impact on provincial

jurisdictions, national standards, and cost-shared funding programs like the Canada Assistance Plan. In the context of privatization of social services, one can see management services in the CUSFTA as providing a 'trojan horse,' the 'thin edge of the wedge,' for ultimately privatizing, to the point of commercializing, substantial numbers of health and social services. Otherwise, why does one include a service sector in the CUSFTA which, up to now, has rarely been considered for generating profits? Surely placing social services in the CUSFTA at this point must be more a political matter than one of economics.

While I do not pretend to comprehend the magnitude of the matter, the nagging question remains: "Why are substantial segments of the personal social services named in the Agreement?" Knowing that economic and social policy go hand-in-hand, I am concerned about the management of social services under the CUSFTA. I know that the mood of some political leaders in Canada is toward privatization. Consequently, there is a parallel process of privatization underway in human services across Canada, from devolution of government service delivery to community-based organizations to outright commercial interests. The Meech Lake Accord decentralizes government powers to the point that social welfare is now to be moulded almost exclusively at a provincial level. The Accord, plus the "ground-breaking" effort by the CUSFTA to include services as a newly acclaimed 'trade commodity' causes one to ask where Canada is heading. The issue of social services and the CUSFTA may be of small import in the equation, but the fact that social programs are in the equation at all should be of concern to those who believe that they are, indeed, 'sacred trusts."

THE CANADA-U.S. FREE TRADE AGREEMENT AND LABOUR ADJUSTMENT: A SENSE OF PERSPECTIVE

Paul K. Gorecki[1]

The signing of the Canada-U.S. Free Trade Agreement (CUSFTA) has generated much debate and thought over a wide range of issues. One of these is that of adjustment in general and labour adjustment in particular. Concerns are expressed that, although most econometric estimates show that the CUSFTA will lead to overall economy-wide job gains,[2] many jobs may be lost; certain industries, including several already subject to considerable pressure from imports, likely will experience net job losses; and specific classes of workers in given localities may encounter particular difficulty finding new jobs.

In part, because of such concerns, the federal government has created a Council on Adjustment (in January 1988) to advise on how workers and firms can best "meet...[the] challenges"[3] of the CUSFTA, including the possibility, "that some industries or firms will contract while others are expanding."[4] One leading labour leader, who is also a member of the Council on Adjustment, has publicly called for "a major adjustment package" of government measures in response to the Agreement.[5]

However, adjustment is not new. To paraphrase the Greek philosopher, Heraclitus, if there is one constant in economic life it is, paradoxically, change. Interest in adjustment as a public policy issue has increased substantially in the 1970s and 1980s in Canada and among other members of the Organization of Economic Co-operation and Development (OECD). Much of this interest reflected sluggish economic growth, high unemployment rates, perceived resistance to structural change, and the resort to new protectionist measures by many countries following the first OPEC oil shock of 1973-74. While Canada shared this concern, the advent of the CUSFTA has heightened interest in the adjustment issue.

In addressing the issue of the CUSFTA and labour adjustment, the critical question revolves around the extent of adjustment problems and the appropriate public policy response. An adjustment problem arises if, for example, as a result of the CUSFTA, workers experience longer periods of unemployment than they would otherwise. This is likely to be the case where the Agreement results in a plant shutdown where there are few other employment opportunities. This will lead to private losses of foregone income and perhaps, if the unemployment is localized, declining property values. At the level of society, the loss will consist of foregone output which will likely be increased if the laid-off workers add to an already large existing pool of unemployed.

In order to address the question of the Agreement and labour adjustment, we draw upon the record of adjustment in Canada. This record refers not only to the response of workers and firms to the pressures for change, but also of governments. Much of this record has been examined and discussed by the Economic Council of Canada in its recently released statement, Managing Adjustment: Policies for Trade-Sensitive Industries, on which this paper draws heavily. It is only by examining the broad canvas of change that a sense of perspective can be gained.

Adjustment Pressures

Over the past 25 years there has been a large number of pressures to which Canadian workers, firms and governments have had to respond. Some of these pressures were trade-related, others less so. They include:

- the rise of the newly industrialized countries (NICs) which, in the current OECD definition, include South Korea, Hong Kong, Singapore, Taiwan, Brazil and Mexico. This has posed a challenge to many of Canada's traditional industries -- textiles, clothing and footwear, in particular;

- the pace of technological change, which has forced Canadian firms to adopt newer technology in order to keep up with foreign rivals, and has forced workers to retrain or otherwise acquire new skills;

- a fluctuating exchange rate, which has affected Canada's competitiveness vis-à-vis the major

industrial countries, leading producers to make judgements as to the permanency of the change and to react accordingly;

- the deregulation of the railway, trucking and airline industries in the United States in the late 1970s and early 1980s, which put pressure on Canada to deregulate so as not to place large users of transportation services at a competitive disadvantage relative to their U.S. counterparts;

- the decline in tariffs under the Kennedy Round (1966-70) and the Tokyo Round (1979-87) of the General Agreement on Tariffs and Trade (GATT), which has increased import competition for Canadian producers because the prices of imports have fallen. At the same time, it has provided opportunities for the realization of scale economies resulting from greater access to foreign markets;

- the growth of the Japanese economy, which has posed a competitive challenge to Canadian producers of commodities -- automobiles, ships and electrical goods, in particular -- where capital, high-wage skilled labour and/or R&D are important inputs;

- the decline in transportation costs, combined with easier access to labour in Third World countries, which has provided opportunities for Canadian corporations to locate plants abroad or to subcontract operations to foreign firms; and,

- the trebling of the world price of oil in 1973-74, its subsequent doubling in 1978-79, and more recently, its substantial decline -- changes that have placed considerable pressure on Canadian producers to use more flexible, fuel-efficient methods of production in order to compete internationally.

These and other pressures have led to an increase in the importance of trade to the Canadian economy. For example, in the manufacturing sector imports have risen from 21 per cent of domestic consumption in 1966 to 36 per cent in 1984. Over the same period in the manufacturing sector, Canadian exports rose from 19 to 36 per cent of domestic shipments.[6] The pressures on Canadian firms and workers to meet the challenge of international competition are likely to continue in the future. They will include:

- a continuing fall in tariffs and a greater openness of markets because of the changes currently being discussed under the Uruguay Round of the GATT negotiations, which is scheduled to be completed by 1991;

- the movement of NICs out of labour-intensive commodities into more skill and capital-intensive products, and their replacement by the 'next-tier' NICs, such as the "ASEAN Four" (Association of South-East Asian Nations) -- Malaysia, Thailand, the Philippines, and Indonesia -- as well as China; and,

- the prospect of a Canada-U.S. Free Trade Agreement, which has awakened many Canadians to the scope of the adjustment facing sectors of the economy that engage in international trade. In the case of the manufacturing sector, this will see tariffs, which in 1985 averaged 3 per cent, be gradually phased out over a period of up to 10 years, starting January 1, 1989.

There will, no doubt, be other pressures for change which we cannot predict today, any more than in the late 1960s the oil price rises of the 1970s or the U.S. transportation deregulation were generally expected to take place.

All of these changes, both past, present and future, put pressure on Canadian workers (to change occupations, employers, localities and so on) and firms (to exit an industry, to revitalize and meet the competition by designing better products through improved quality control and marketing strategies and so on). Some of the past pressures are likely to continue with equal, if not heightened, force. For example, the NICs, the 'next-tier' NICs and China will probably provide significant import competition in such industries as clothing, shipbuilding, textiles and automobiles. In this context, it is not at all clear that the proposed CUSFTA is the most important labour adjustment problem facing Canada or that it deserves separate, special attention in terms of adjustment programs. Indeed, too much concentration on the CUSFTA may divert attention from much more worrying labour adjustment problems.

Adjustment Responses

We consider the record of adjustment to the pressures of change by firms, workers, and governments. Since our emphasis is on labour adjustment, in our discussion of

firms we will focus on the job implications of their activities, while in discussing government policy, attention will focus on labour adjustment policies. Much of our attention is directed toward the manufacturing sector. The Council's examination of the CUSFTA suggests that it is this sector that will bear the burden of labour adjustment -- in the sense that it is only manufacturing, not service or primary sector industries, that will experience actual net job losses as a result of the effects of the removal of trade barriers and the consequent productivity gains.

Firm-Initiated Job Change[7] The creation, expansion, contraction or closing down of firms has led to consequent job loss and job gain. An examination of 'Census of Manufacturing' data from Statistics Canada shows that each year a large and relatively constant proportion of jobs in Canada's manufacturing sector disappear as a result of the decline or closure of manufacturing plants -- over 8 per cent per year on average during the 1970s. In contrast, the annual increase in the number of jobs created in manufacturing by newly created or expanding establishments was over 9 per cent. Thus, although the annual net increase in the number of manufacturing jobs is less than one per cent, there is considerable continuing underlying change.

Worker-Initiated Job Change[8] The worker response to change can be examined by looking directly at the number of workers who leave their employers. These separations are either temporary (when the workers return to the same employer within two years, the cut-off used in the data source) or permanent. 'Worker separations' can be divided into two different but related components -- displacement and attrition.

Displacement refers to firm-initiated layoffs. An analysis of administrative data supplied by the Department of Employment and Immigration shows that the number of permanent layoffs in any given year is at least as large as the 8 per cent of jobs that disappear each year. This means that the annual establishment-based job-loss rates that we have observed, reflect firm behaviour that results in workers being laid off permanently, rather than short-term reductions in employment after which workers return to the same employers.

Attrition, on the other hand, is worker-initiated, although it may sometimes be caused indirectly by the

decline of a firm, which leads workers to anticipate a layoff and thus leave their jobs. It is divided into several categories for administrative purposes: labour dispute; return to school; illness/injury; quits; pregnancy; early retirement; and, other. The same administrative data show that on an annual basis over the period 1974-82, 'quits' was the primary cause of attrition.

Attrition is a component of worker turnover that is not captured by the establishment-based job-turnover measures, nor by displacement estimates. While an establishment may reduce its work force by eliminating jobs, workers may also leave their employers voluntarily. In doing so, they contribute to the adjustment process. It is therefore important to measure the magnitude of attrition, in order to have a more comprehensive view of the volume of labour market reallocation that the economy manages to absorb each year.

The results show that when measured on an annual basis, worker-initiated attrition is approximately as important as all firm-initiated layoffs, whether permanent or temporary. When the temporary component is removed from both sets of figures, we find that permanent layoffs and permanent attritions together amount to more than 20 per cent of employment annually in the manufacturing sector. The conclusion is inescapable: a very large number of people change jobs and employers in the manufacturing sector each year, either for personal reasons or because of changing economic conditions.

To fully appreciate the degree of adaptability displayed by Canadian workers, we have to supplement the aggregate data on labour market turnover with information on worker mobility. A large turnover of workers does not necessarily prove that they adapt easily. If workers who leave one employer move to another one in the same industry who is offering work in a closely related occupation, it may be difficult for them to adjust should that industry undergo a long-term decline in activity resulting from structural change in the economy. On the other hand, if workers move to other industries, occupations, or regions relatively frequently, we can expect adjustment to be less painful. The degree of mobility thus provides indirect evidence of the adaptability of the labour force.

A considerable body of evidence (drawn from a variety of sources and including administrative data, special sectoral surveys, and a supplement to Statistics Canada's Labour Force Survey) is available on the mobility of the Canadian labour force. Studies of the shipbuilding, steel, footwear, clothing, textile, automobile (and auto parts), and electrical/electronics industries examined the movement of workers into and out of each industry, in terms of their sector of origin and their destination. These and other studies also addressed the issue of regional mobility. The degree of worker mobility across occupations and employers was investigated by tracking individual workers over time. Finally, the experiences of workers who moved were examined according to different age categories, using various indicators such as changes in rates of pay, the time needed to find another job, the duration of any subsequent job, and so on.

The evidence on labour mobility is consistent with the view that workers show considerable mobility between employers, industries and occupations when they leave one job for another. That is not to deny, however, that adjustment problems are likely to be more acute in cases where the industrial base is narrow, or where older workers are particularly affected.

Government Policy[10] Governments in Canada have introduced labour programs to socialize some of the most important risks associated with change. By reducing these risks, society not only reduces the burden of change but may also make change more acceptable. These programs usually provide insurance in varying degrees because of loss of employment (unemployment insurance) and, to a much lesser extent, loss of skills (training assistance), or the changing distribution of job opportunities across the country (mobility allowances). They also promote planning for change, both in general (UI) and at the company level (industrial adjustment service). Such programs are usually offered irrespective of the reason for the loss in employment: technological change; import competition; adverse macroeconomic developments; an over-valued dollar; or, firm bankruptcy.

In a number of instances, however, governments have supplemented these universal or framework programs that apply to many, if not all, sectors of the economy with ones aimed specifically at individuals located in a small number of trade-sensitive industries: for automobile workers, 1965-76; for textile and clothing

workers, 1971-86; and, for footwear and tanning workers, 1978-86. In addition, in the early 1980s, there were programs aimed at communities experiencing economic dislocation because of their dependence upon a small number of industries which were undergoing permanent, not cyclical, change -- the Industry and Labour Adjustment Program, followed by the Modified Industry and Labour Adjustment (1981-87). While the dislocation could be due to any cause, including trade, several community/industry designations were made involving industries -- shipbuilding, automobiles, and pulp and paper -- that were receiving sectoral assistance related to difficulties experienced in meeting foreign competition.

These sectoral labour programs tried to encourage worker adjustment in the targeted industries by two methods: pre-retirement benefit programs in the form of income payments to displaced older workers with a long attachment to a particular industry and little prospect of finding another job; and, re-employment measures designed to encourage job mobility, relocation and retraining so that workers can enter new industries, occupations or places of employment. Such measures can be justified on equity grounds, in the case of older workers who have developed a skill specific to one industry, and on efficiency grounds, in the case of re-employment measures where the decline in industry employment may have led to local labour market congestion problems. Furthermore, as noted above, the evidence suggests that older workers and those in areas with a narrow industrial base face particularly difficult problems in adjustment to change.

Implications

We began this paper by posing the question as to whether there is likely to be a labour adjustment problem because of the CUSFTA and, if so, what the appropriate public policy response should be. An adjustment problem may exist if the concerns expressed in the opening paragraph of this paper have a firm foundation. However, that does not necessarily mean additional adjustment programs; this depends upon their adequacy in dealing with adjustment problems.

Preliminary work by the Council, published in September 1987 in the Twenty-Fourth Annual Review, examined the potential employment effect of immediate implementation of a comprehensive bilateral trade agreement. The September analysis indicated that total

employment changes (both gains and losses) would not be large in the context of the high degree of job and labour turnover detailed above.[11] It suggested that close to 23,000 jobs would be lost economy-wide each year through permanent layoffs and 66,000 jobs created. The permanent layoffs induced by such a comprehensive free trade agreement would account for only 2 per cent of the layoffs that occur normally in each year. This is not an altogether surprising result, in view of the generally low levels of tariffs between Canada and the U.S. In cases where Canadian tariffs are high, they are also frequently high in the U.S., with the aim of combating imports from countries such as the NICs or Japan.

The actual trade agreement announced in October and signed by the heads of government of the two countries in early January 1988 is more limited in scope and will be phased in over 10 years. The Council is currently assessing the impact of the CUSFTA. The indications are that the predicted job loss will be even lower than the September analysis suggested, while the overall job gains will be somewhat more modest.[12]

Nevertheless, despite these results it would be inappropriate to assume that there will be no labour adjustment problems in the late 1980s and early 1990s. Several of the industries projected to suffer a decline, albeit marginal, because of the CUSFTA -- leather, textiles, knitting mills, electrical products -- have been singled out in the past for special government programs because they were perceived to suffer adjustment problems due to international competitive pressures. As noted in our earlier discussion, these pressures -- from the NICs, the next-tier NICs, and Japan -- are likely to continue. Hence, it is important to get adjustment policies right. The CUSFTA, by focusing the debate on the adjustment issue has, one hopes, increased the probability that appropriate policies will be introduced to deal with this important problem.

In the Council statement on adjustment, a set of principles are set out based on the record of the past. In general, the principles call for assistance to workers not firms, and careful, but limited, use of quantitative restraints on imports. These principles were designed to correct some of the policy problems of the past, particularly the fact that sectoral subsidy programs and quantitative restraints on imports tended to inhibit and retard rather than promote adjustment. A

side effect of this was that the sectoral labour adjustment policies were not heavily used as part of an effort to facilitate adjustment to international competition.

In terms of labour policy, the conclusion is that governments should use framework, not sector - specific policies. (Indeed, in general, the preference was for framework not sectoral policies.) One of the reasons for this preference is the practical difficulties of separating out trade-displaced workers from others, as well as the equity problems of singling out CUSFTA-displaced workers. While a complete review of all labour policies was not undertaken, suggestions were made for the implementation of the Program for Older Workers -- a framework policy to correct some of the problems associated with previous sectoral pre-retirement benefit programs -- and greater use of the Industrial Adjustment Service to facilitate adjustment. In addition, programs such as that initiated in the steel industry via the Employment and Adjustment Committee of the Canadian Steel Conference, seem to hold out much promise. In this case, under the National Labour Market Innovations Program (part of the Canadian Jobs Strategy) funds have been allocated to the Steel Conference to design better adjustment programs for displaced workers.

One prevalent characteristic of some of the most important trade-sensitive industries is that worker education is low, by general manufacturing standards, and the jobs are unskilled. For example, 76 per cent of the workers in Ford's automobile assembly plants in Canada are in unskilled jobs (defined as those requiring less than 30 days training to be proficient on the job). In 1981, the percentage of the labour force with less than Grade 9 education was much higher in the textile, leather, knitting and clothing industries--ranging from 26 per cent to 39 per cent -- than in all of manufacturing, where it was only 19 per cent. Furthermore, this lack of formal education is particularly prevalent in the clothing industry -- by far the largest employer of the four industries -- where the labour force consists largely of women, many of whom are immigrants with little command of English. Indeed, this issue was raised by one labour representative at a recent conference in the context of the CUSFTA.[13]

Canada is unlikely to have a competitive advantage in industries characterized by low levels of formal education and unskilled tasks. Underdeveloped countries

and NICs have large supplies of labour with such characteristics. Furthermore, even in industries requiring considerable capital investment (such as the automobile industry), some of the NICs (South Korea, for example) pose a competitive challenge to Canadian producers. This does not mean that trade-sensitive sectors cannot revitalize themselves using a more skilled work force. Nevertheless, job growth in Canada is likely to be in sectors requiring more highly skilled labour, so it is important that workers be given the opportunity to upgrade their skills and their educational attainment.

In Making Technology Work,[14] the Council pointed out that the need for skill upgrading is not confined to trade-sensitive industries. In that report, we made a number of suggestions for achieving a well-trained, flexible and committed labour force. These included support for employer-based training in selected highly skilled occupations, the creation of conditions conducive to continuous learning on the job, and the provision of funds and leave for training. The central principles of the Council's proposed policy framework for worker retraining were: private-sector initiative in making training choices; support for joint employer/employee solutions; concern for those disadvantaged in the labour force; flexibility in program design and administration; and, decentralized decision making.

These principles are consistent with the general orientation of policies promoting adjustment, particularly in encouraging workers and employers to make their own decisions about training.

Regarding government funding for labour training, the Council suggested in Making Technology Work, not so much an increase but a reallocation of funds, with a view to providing "an environment within which employers and workers can make informed decisions about necessary retooling[15] and can then carry out the required training."

NOTES

1. Much of the material reported herein appears in Economic Council of Canada, 1988a. However, the views in the paper are those of the author alone and do not necessarily reflect those of the Economic Council of Canada. R. A. Jenness provided useful comments on an earlier version.

2. See, for example, Economic Council of Canada, 1987a.

3. Government of Canada, 1988, p. 1.

4. Ibid., p. 1.

5. McCambly, 1987, p. 181.

6. Department of Regional Industrial Expansion, 1985, Report 1.

7. For details, see Baldwin and Gorecki, 1988; and, Economic Council of Canada, 1988a and 1988b.

8. For details, see Baldwin and Gorecki, 1988; Economic Council of Canada, 1988a and 1988b; and, Robertson, 1987.

9. For details, see Economic Council of Canada, 1988b, Chapter 3.

10. For further discussion, see Economic Council of Canada, 1988b, Chapter 7.

11. See also Economic Council of Canada, 1987a, pp. 40-42.

12. For details, see Economic Council of Canada, 1988c.

13. Surich, 1987, p. 200.

14. Economic Council of Canada, 1987b.

15. Ibid., p. 31.

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DISCUSSANTS

Shirley Seward

I wish to highlight some demographic trends which may affect labour force adjustment subsequent to the free trade agreement.

A wide range of projections of the future population and labour force has been developed by federal government departments, and by individual researchers. On the basis of these projections, the demographic trends projected over the coming decades will follow the patterns established in the 1970s and 1980s. The overall rate of population and labour force growth will decline steadily; the proportion of the population under the age of 20 will fall; the proportion aged 65 and over will rise; and the labour force will continue to age.

A labour force that is growing more slowly will mean fewer young labour market entrants in the late 1980s and the 1990s. According to research undertaken by the Institute for Research on Public Policy, there were, in 1981, over 3 million youths in the Canadian labour market, representing more than one-quarter of the labour force. By 1985, their share had dropped to 22.6 per cent. By the end of the century, given current participation rates, their share might fall to 17 per cent. This decline in the relative number of young labour market entrants could lead to a labour force that is less flexible and mobile from a geographical, occupational and industrial perspective.

To a certain extent, the smaller number of new labour market entrants could be offset, at least until the end of the century, by gains expected to be reaped from the presence in the labour force of the large, gradually aging and relatively well-educated baby boom generation whose members are now in their twenties and thirties. Major investments were made in educating the members of these cohorts, and one would logically expect a payoff from such an investment, particularly as workers gain on-the-job expérience. However, three caveats should be noted in discussing the potential productivity gains associated with the presence of the baby boom generation in the labour force. First, the education obtained by the current labour force in the 1950s and and 1960s, may well be inappropriate in the late 1980s and 1990s, particularly given the changing economic environment and technological change. Secondly, training and retraining to update skills and facilitate adjustments are of critical importance. This suggests that governments may

have to expend more resources on such programs as the labour force continues to age. Thirdly, the aging process may make the baby boom labour force less mobile -- from both an occupational and a geographical perspective -- thereby impeding the adjustment process.

What do these demographic trends mean in the context of a free trade agreement? First, the assumption that workers adjusted in the past, and therefore will have no problem adjusting in the future is superficial. We have seen, through labour tracking studies, that vulnerable workers, such as older workers, less educated workers, and women, have not adjusted as easily as other groups. Also, because the labour force is aging, and there are few young recruits, it may be less flexible and adaptable.

Secondly, in view of the differences in the demographic profiles in industries and occupations, one single umbrella approach to labour market adjustment such as the Canadian Job Strategy, is not likely to be enough. We need instead programs aimed at particular demographic groups and particular industries. One such group is comprised of immigrant women. Those who enter occupations like the clothing industry do not have access to subsidized language training provided by Employment and Immigration. The reason is that we assume they do not need to speak one or more of the official languages in order to work in the clothing industry. That, to me, is short-sighted. Personally, I think they need the official language skills to work in any industry and simply to live in Canada. Furthermore, if we are thinking of adjustment, we have to make sure the basic language skills are there before we can hope to train people within vulnerable sectors. In addition to programs targetted to particular demographic groups, it is essential that we develop innovative approaches to different sectors. One interesting example is the approach developed by the Canadian steel industry where labour and management are working together to provide labour adjustment assistance to displaced workers. Such an approach has great potential and may point the way to more effective labour adjustment programs in the future.

Peter Bakvis

The basic assumptions behind the Economic Council's approach to labour adjustment under free trade are that there will be more job gains than job losses; that the repercussions of the Agreement will be marginal compared to regular job losses; that policies should be directed to worker mobility rather than propping up declining industries; and that no radical new adjustment programs are necessary.

The difficulty with these assumptions is that they do not hold up under scrutiny. The estimates of gains from free trade, for example, have been accompanied by falling expectations with each successive study. The 1985 Cox-Harris study for the Macdonald Commission projected 650,000 jobs from free trade. The 1987 Economic Council study forecast 350,000. The recent 1988 study of the Department of Finance reduced the projected gains to 120,000. There are problems with all of these studies. They exclude services from the model, and they make very liberal assumptions about productivity gains. They do not take into account U.S. countervail. If any one of the assumptions is changed only marginally, the potential gains projected by the studies, slight as they are, could turn into net losses. The potential for job losses, particularly in sensitive sectors, was confirmed in a recent Quebec government study.

Putting aside the viability of the macroeconomic gains, what are the prospects for the mobility of labour? As Shirley Seward noted in her remarks, the labour force of Canada is aging. The aging process will adversely affect the capacity of displaced workers to adjust. Furthermore, if the major growth from free trade takes place in non-unionized, low-wage sectors, the incentive for displaced workers to move will be reduced. In addition, the problems of displacement will likely be compounded by sectoral or regional concentration of job losses, which will be very different from the regular turnover of essentially younger workers during the seventies. Such losses are probable in areas like machinery, electrical and electronic products, and food products.

I do not think that present mobility and support programs, such as unemployment insurance, are adequate to reply to the kind of dislocation problems that could occur from free trade. We shall need sectorally and regionally specific adjustment programs if the CUSFTA is

put in place. At the same time, it is not clear, nor does the Econimic Council address the question of the extent to which governments will be tied by the Agreement. Already, there have been cutbacks in labour adjustment benefits programs, and programs for older workers, as well as regional development grants.

Ken Hart

I want to talk about two points. One is job mobility and the adaptability of the labour force in the face of both the free trade agreement and changes in labour markets generally. The second is regional mobility and demographic policy.

If we look at corporate plans for adjustment to free trade, what we see is what you would expect -- companies shifting from relatively low product lines to stronger lines, as well as a fair amount of reinvestment and an increase in the technological level of the workers generally. What we come to is whether, because of free trade or technological change, we need to make a radical change in the way labour is prepared for the workplace. I would suggest that we have to go beyond talking about keeping youth in school or sending people back to school. I think we are also going to have to look at some new institutional arrangements. In the past, we have been protected by a relatively high Canadian dollar. We have always been able to bring people into the country who were well trained. They could come here and enjoy a high standard of living even in a society that was not as productive as it might have been because of the high dollar. In the future, we shall not be able to do that. Because we are not training people properly, we are facing shortages of some significant skills. If we try to put in place massive federal programs to predict training needs, we are going to repeat ridiculous mistakes we have made in the past, when we were turning out people who were ill-equipped by the time we got them out the door. On the other hand, if we ask business to take on the load of training people, we are going to get the response that it's a very mobile population. So what we need to do in the face of free trade constraints and technological change is to develop a new way of promoting the ownership of skills.

With regard to my second point, it is important to recognize that Canada has typically chosen demographic policies of adjustment that involved paying people to stay where they did not have jobs. The United States

has typically chosen demographic adjustment policies of letting huge population movements take place, whether from the deep south to the industrial north, or from the industrial north to the south-west. In general, human mobility has been chosen down there, and up here, transfer payments have been chosen. We now seem to be at a point in our history when we are making a change. The rapid growth of Toronto is an example. I don't recall a national debate on whether this was the appropriate direction to go for labour adjustment but we are falling into it, partly on the basis of slogans about free market versus intervention. I think that the change needs to be discussed in a general social policy context.

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